Supreme Court, U.S.
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No.

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1993

JOHN MARTIN-MUSUMECI,
Petitioner,
vs.
LAW OFFICES OF HERBERT HAFIF
PENSION AND PROFIT SHARING PLAN,
Respondent.

PETITION FOR WRIT OF CERTIORARI

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64 pp

QUESTIONS PRESENTED

1. Is it just and proper for the United States Court of Appeal for the Ninth Circuit to render an unpublished decision concerning the interpretation of a statute of the Uniform Commercial Code in order to avoid having that decision become precedent where that decision involves an unsettled area of commercial law of great importance and is directly contrary to the express language of the statute and to the intent of its drafters.

2. Under Section 9505(2) of the Uniform Commercial Code, can a party "strictly foreclose" on a general intangible?

LIST OF PARTIES

Petitioner: John Martin-Musumeci, an individual.

Respondent: Law Offices of Herbert Hafif Pension and Profit Sharing Plan, an ERISA qualified pension plan maintained by the Law Offices of Herbert Hafif, a business entity, form unknown.

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PETITION FOR WRIT OF CERTIORARI

STATEMENT OF JURISDICTION

This petition for a writ of certiorari is based upon an unpublished decision of the United States Court of Appeals for the Ninth Circuit which was entered on March 10, 1994. The jurisdiction of the United States Supreme Court is invoked under 28 U.S.C. Section 1254(1) and Rule 10.1(a) of the Rules of the Supreme Court of the United States in that, in rendering an unpublished decision as to the meaning of a statute in an unsettled area of great importance to commercial law, the United States Court of Appeal for the Ninth Circuit has "so far departed from the accepted and usual course of judicial proceedings, or sanctioned such a departure by a lower court, as to call for an exercise of this Court's power of supervision."

STATUTES INVOLVED

Uniform Commercial Code Section 9-505(2) (West Pub. Co. 1994):

> In any other case involving consumer goods or any other collateral a secured party in possession may, after default, propose to retain the collateral in satisfaction of the obligation. Written notice of such proposal shall be sent to the debtor if he has not signed after default a statement renouncing or modifying his rights under this subdivision. In the case of consumer goods no other notice need be given. In other cases notice shall be sent to any other secured party from whom the secured party has received (before sending his notice to the debtor or before the debtor's renunciation of his rights) written notice of a claim of an interest in the collateral. If the secured party receives objection in writing from a person entitled to receive notification within 21 days after notice was sent, the secured party must dispose of the collateral under Section 9-504. In the absence of such written objection the secured party may retain the collateral in satisfaction of debtor's obligation.

I.

STATEMENT OF THE CASE

A. Background:

On July 11, 1984, Herbert Hafif, an attorney, made a loan to Debtor, John Martin-Musumeci ("Debtor"), who was then his client, in the amount of $350,000. This loan was made out of funds held by the Herbert Hafif Pension and Profit Sharing Plan ("Hafif"). Debtor executed a note in favor of Hafif, secured by a two percent interest of the undivided beneficial interest in the Marriner Note Trust ("Trust").

The Note provided that in the event Debtor failed to make any interest installment payment when due, Hafif, within 90 days of making a written demand for payment, could sell the two percent interest in the Trust ("2 Points"). The Note provided that if the 2 Points were not sold within the 90 day period, then "full title to said security shall transfer to the Holder [Hafif] and shall be deemed full satisfaction of the entire obligation; I [Debtor] shall not be liable for any real or alleged deficiency." As an alternative remedy, the Note provided Hafif with the right to convert one-half of one percent of the interest in the Trust as repayment.

In a letter dated October 11, 1984, an employee of the trustee of the Marriner Note Trust acknowledged Hafif's security interest in the 2 Points.

Hafif sent Debtor a letter dated March 13, 1985 stating that Hafif was accelerating payment of the loan pursuant to the terms and conditions of the Note. The letter stated that: "[w]e certainly do not wish to exercise our right of conversion." However, the letter made no reference whatsoever to any action Hafif intended to take with respect to the 2 Points.

In a letter from Hafif to Debtor dated August 13, 1985, Hafif notified Debtor that Hafif: ". . . has foreclosed on the security." Further, Hafif stated in the letter that "[w]e deem the foreclosure final with title to the security vested in the Pension Plan." This letter was the first notice that Debtor received which actually stated that Hafif had elected to retain the 2 Points in satisfaction of the Note but it did not provide Debtor with any opportunity to object to this retention but rather presented it as a fait accompli.

Upon receipt of the August 13, 1985 letter, Debtor immediately informed Hafif that he objected to the "foreclosure" of the 2 Points as provided in the letter. In a letter

from Hafif's employee to Debtor dated August 25, 1985, Hafif's employee acknowledged that Hafif had received Debtor's objection, stating that: "[Hafif] was a little bit furious when you claimed that he [Hafif] hadn't properly foreclosed.... Now that you [Debtor] have given up on that idea and agreed that the plan owns the stock, he's [Hafif's] given you the right to get it back." The letter also stated: "[Hafif] is now the full owner of the 2 Points," and advised Debtor that he could repurchase the 2 Points from Hafif for the principal and interest due.

B. Bankruptcy Action:

In 1988, Debtor filed for bankruptcy under Chapter 11 of the United States Bankruptcy Code. The bankruptcy was originally filed in Hawaii but was subsequently transferred to the Northern District of California. On July 5, 1990, Debtor brought an adversary proceeding against Hafif, Adv. No. 4-90-0241AT (later consolidated with Adv. No. 4-90-0247-AN), seeking to recover the 2 Points on the basis that Hafif had violated the California Commercial Code in foreclosing on the 2 Points and retaining it in lieu of the amount due under the Note without complying with the requirements of Section 9504 and Section 9505 of the California Commercial Code.

On August 30, 1991, Hafif prevailed at trial before the Honorable Randall J. Newsome, Bankruptcy Judge United States Bankruptcy Court for the Northern District of California and a final judgment was filed on September 3, 1991 ("Judgment"). In ruling in Hafif's favor, the Bankruptcy Court stated that, while the collateral was a general intangible, and was thus not susceptible to possession in the usual sense, Hafif's receipt of an acknowledgment of its security interest in the collateral from the trustee of the Trust was sufficient to constitute a constructive possession and that this constructive possession was all that was needed for

Hafif to strictly foreclose under Section 9-505(2) as that section did not affirmatively exclude general intangibles from its reach. The Bankruptcy Court also expressly found that the collateral for the Note (the 2 Points) had a value of $1,400,000 at the time of the purported "strict foreclosure"—in other words, well in excess of the amount Hafif claimed under the Note: $350,000. Debtor unsuccessfully moved to alter the Judgment under Bankruptcy Rule 9023 and thereafter timely appealed to the District Court.

C. The District Court Affirms In An Unpublished Order:

The District Court's jurisdiction was founded upon 28 U.S.C. Section 158(a) and Bankruptcy Rule 8001(a). On July 30, 1992, the Honorable Barbara A. Caulfield, Judge of the United States District Court for the Northern District of California ("District Court"), issued an order affirming the Judgment ("Order") on the bases of both of the Bankruptcy Court's findings: that constructive possession existed and sufficed *and* that Section 9-505(2) in fact allowed for strict foreclosure of general intangibles. This Order was entered on July 31, 1992, but was never published, and Debtor appealed on August 27, 1992.

D. The Ninth Circuit Also Issues an Unpublished Decision:

Appellate jurisdiction in this action was founded upon 28 U.S.C. Section 158(d), providing courts of appeal with jurisdiction to hear appeals from final decisions, judgments and orders of district courts entered under Section 158(a) (governing appeals from final bankruptcy court decisions, judgments and orders).

On March 10, 1994, the Ninth Circuit, over a dissent by Judge Noonan, issued an *unpublished* memorandum opinion affirming the Order ("Memorandum"). The majority in this Memorandum stated, in pertinent part, that, while they

agreed that a general intangible cannot be possessed for purposes of Section 9-505, they found an exception where there has been an acknowledgment of the security interest by a third party trustee. In dissent, Judge Noonan observed that since, as the majority acknowledged, a general intangible cannot be possessed, then it cannot be subject to strict foreclosure under Section 9-505.

II.

ARGUMENT

1. It Is Unjust And Improper For A Court Of Appeal To Decline To Publish A Decision In An Important, Unsettled Area Of Statutory Interpretation In Order To Avoid That Decision Becoming A Precedent:

The appellate courts function not only to rule on cases affecting individual parties, but to set precedent affecting the law within an entire circuit. Thus, a decision of a Court of Appeals, and the rationale on which it is based, is of interest to all of society. With such a great responsibility, it is imperative that when faced with a decision of public importance, an appellate court not only make society aware of its decision, but also publish the rationale of the decision. This is particularly true where, as here, there is a dissent which goes to the heart of the court's decision.

A. By Failing To Publish The Decision Below, The Ninth Circuit Is Shirking Its Judicial Duty:

Under Ninth Circuit Rule 36-1, all opinions are to be published but memoranda are not. Thus, the only way for the Majority to *avoid* having its decision published was for it to designate that decision as a "memorandum." Considering the criteria for designating a decision as an "opinion," as set

forth by Ninth Circuit Rule 36-2, the instant decision clearly should have been designated as an "opinion":

> A written, reasoned disposition shall be designated as an OPINION only if it:
>
> (a) Establishes, alters, modifies or clarifies a rule of law, or
>
> (b) Calls attention to a rule of law which appears to have been generally overlooked, or . . .
>
> (d) Involves a legal or factual issue of unique interest or substantial public importance . . .

A decision needs to meet only one of these criteria to warrant being published. The Memorandum here meets each of these conditions as it marks a dramatic departure from the statutory language and general interpretation of Section 9-505, either because it is a new rule or a generally overlooked old rule, and impacts a broad range of commercial transactions and would thus be of great interest and concern to the business community.

However, by using the designation "Memorandum," the Majority has ensured that its decision will neither be seen nor cited by other members of the business community. *See* Ninth Circuit Rule 36-3.

As Gilbert S. Merritt, Jr., the Chief Judge of the Court of Appeal for the Sixth Circuit, recently stated, in discussing his decision to reverse the Sixth Circuit's ban on the citation of unpublished opinions: "The law needs to be visible to the public, and judges need to be accountable to the public, ..." Richard C. Reuben, *New Cites For Sore Eyes*, ABA Journal, June, 1994, at 22 (quoting Judge Merritt). When an appellate court fails to publish its opinion for the public to read and critique, it has failed in this duty. The result is often an opinion that is not well reasoned, and a ruling that is simply incorrect. As other noted commentators

have recognized: "The danger here is that the decision not to publish will affect the reasoning or even the result." William L. Reynolds & William M. Richman, *An Evaluation of Limited Publication in the United States Courts of Appeals: The Price of Reform,* 48 U. Chi. L. Rev. 573, 581 (1981) [hereinafter, Limited Publication].

The perfunctory analysis of the Majority in the Ninth Circuit's Memorandum here hardly serves the goals expressed above; to the contrary, it reinforces the need for those goals by at least suggesting that either the Ninth Circuit issued a result-oriented opinion which it knew to be contrary to the law and public policy, or that it issued a significant ruling which changed the rules of conduct in an important area of commercial law — and which thus would have deserved a full, well-reasoned opinion to guide parties and their counsel in future business dealings and litigation. Unfortunately, the likelihood that it was the former is increased by what little analysis is provided.

Although the Majority in the Ninth Circuit's Memorandum conceded that an essential element of strict foreclosure under Uniform Commercial Code Section 9-505(2) is that a secured party must be in possession of the collateral, and went on to recognize that the collateral at issue here was a general intangible which, by definition, could not be possessed, nevertheless the Majority blithely went on to find that the requirement of possession was satisfied here. Then, having taken this significant and unprecedented step, which had the potential to completely change the general understanding and application of this statute in the business world, the Majority declared the Memorandum to be "not appropriate for publication." By the paucity of its analysis, and by its declining to have this Memorandum published, the Majority seems to have simply been creating a one-time exception to the statute, which it did not want others to have

resort to as the Ninth Circuit itself believed that it was bad law.

The result of this judicial activism is threefold: First, it undermines the purposes of the Uniform Commercial Code, as discussed in the next section. Second, it usurps the power and duty of the state legislature to adopt and/or draft legislation in the manner it sees fit. Third, depending upon the Majority's reasons for issuing this unpublished Memorandum, it either a) disregards the rights of Petitioner to a fair and well reasoned decision based upon the law, or b) by placing such a decision away from public scrutiny, deprives other business people of a clear understanding of what the Ninth Circuit believes to be the proper interpretation of the law in this area.

Had the Ninth Circuit been required to publish the decision, along with its incisive dissent, thereby subjecting it to public review and criticism, the Majority would have been forced to analyze the issues more thoroughly, and would have either been constrained from issuing a result-oriented opinion which was unsupported by the law, or issued a seminal opinion in this field which should have been published. Instead, the Majority hid its actions behind the shield of nonpublication.

This approach allowed the judges to avoid doing their jobs, relieving them of their responsibility to approach such important issues with the intense thought, zeal, and intellectual effort that they would put forward in a published opinion. A decision made in this manner must be reviewed by this Court to insure that the issues involved were adequately addressed, and to enable this Court to provide guidance to the federal courts as to which opinions can and cannot be certified for nonpublication.

B. Nonpublication Of Decisions Should Be Strictly Limited To Noncontroversial Decisions That Do Not Establish Unique Rules Of Law:

By electing not to publishing the majority and dissenting opinions in the instant case, the Ninth Circuit is disregarding the rationale behind limiting publication of opinions. Commentators have discussed this purpose:

> First are the stated premises of limited publication, which is a treatment supposedly reserved for cases that do not implicate the lawmaking function of the court — routine, uncontroversial cases. Cases that contain dissents or concurrences are, by definition, controversial; . . . Accordingly, few decisions with separate opinions should go unpublished.

Limited Publication, at 612.

In the present case, there is a separate opinion. In his dissent, Judge Noonan readily recognized the flaw in the majority opinion's reasoning: "[a]s the disposition of the court acknowledges, a general intangible cannot be possessed. As possession was necessary under California law for foreclosure, no foreclosure occurred. I would reverse." This reasoning could not be more clear. It takes the plain meaning of the statute and applies it to the facts of the case. Unfortunately, the majority refused to show such judicial restraint. Judge Noonan's dissent goes to the heart of the majority's decision and shows that the opinion is anything but routine or uncontroversial and, as such, it should have been published.

It has also been noted that "[a] court might also use the cloak of nonpublication to avoid the task of reconciling arguably inconsistent decisions." William L. Reynolds & William M. Richman, *The Non-Precedential Precedent — Limited Publication And No-Citation Rules In The United States Courts Of Appeals*, 78 Colum. L. Rev. 1167, 1200

(1978). In the present case, the Ninth Circuit has gone one step further by using the cloak of nonpublication to avoid the task of reconciling the internal inconsistencies of its Majority opinion. The Majority, while recognizing the requirement of Section 9-505(2), that a secured party be in possession of the collateral *before* strictly foreclosing, then chooses to wholly ignore that requirement.

Had the Court of Appeals published the opinion, it is likely that fuller and more critical reasoning would have been employed but, instead, the court chose to use the shield of nonpublication to bury what was either a troubling or at least novel opinion away from public scrutiny and use — a practice that is totally at odds both with the rights of Petitioner and with society's right to access to opinions of the judiciary.

Finally, this Court should follow its rationale for granting certiorari in *Taylor v. McKeithen*, 407 U.S. 191, 32 L.Ed.2d 648, 92 S.Ct. 1980 (1972). There, in a case involving reapportionment, the Court of Appeals had reversed the lower court without issuing an opinion. In granting certiorari, this Court noted that the "record does not fully inform us of the precise nature of the litigation and because we have not had the benefit of the insight of the Court of Appeals, we grant the petition for writ of certiorari . . ." *Taylor*, 407 U.S. at 194. Although the Court, in a footnote agrees that courts of appeal *generally* "have wide latitude in their decisions of whether or how to write opinions," it also recognized that circumstances can arise which make that decision an abuse of discretion and warrant intervention by this Court. *Id.* at n. 4.

Similarly, in the instant case, the unpublished opinion gives little insight into the rationale the Ninth Circuit used to reach this questionable decision. Thus, the petition for writ of certiorari should be granted so that the issues involved in this case can be thoroughly analyzed, and the

rights of the appellant properly addressed, and so that this Court can provide guidance to the lower courts as to the proper uses and abuses of the practice of non-publication.

2. Section 9-505(2), Requires That The Secured Party Be In Actual Possession Of The Collateral, And Does Not Apply To General Intangibles, Which Are Per Se Incapable Of Being Possessed, And A Uniform Application Of This Section Is Necessary In Order To Facilitate Interstate Commerce:

The reason for the Ninth Circuit's disinclination to publish the Memorandum seems clear. As discussed more fully below, such a decision would be bad law and run contrary to the actual intent of the drafters of the Uniform Commercial Code so it should not be allowed to stand as a precedent. In other words, this was a "result" oriented decision, with the Ninth Circuit deciding who it thought should win and then coming up with a rationale to support that determination. This is such a radical departure from the "accepted and usual course of judicial proceedings" that this Court should put a stop to the practice.

Moreover, one of the primary goals of the UCC is to create a *uniform* set of commercial law so that anyone transacting business in one of the states which have adopted the UCC will have the same, or at least similar, rights and obligations in the other states which have adopted it, thereby easing the flow of interstate commerce. UCC Section 1-102(2). *See Connolly v. Bank of Sonoma*, 184 Cal.App.3d 1119, 1125 (1986); *See also Los Angeles Nat'l Bank v. Bank of Canton*, 229 Cal.App.3d 1267, 1278 (1991), quoting *United States Fid. & Guar. v. Federal Reserve Bank*, 620 F.Supp. 361, 370 (S.D.N.Y. 1985) for the proposition that, in terms of its basic purpose: "The UCC . . . was designed to facilitate commerce primarily by

guiding and making predictable the consequences of behavior."

Section 9-505 makes available, under certain conditions and in certain circumstances, the remedy of "strict foreclosure" which was sometimes available under common law. Under strict foreclosure, the secured party retains the collateral in full satisfaction of the debt. Section 9-505(1) provides for strict foreclosure with respect to certain consumer goods, and Section 9-505(2) provides that:

> In any other case involving consumer goods or any other collateral *a secured party in possession* may, after default, propose to retain the collateral in satisfaction of the obligation. Written notice of such proposal shall be sent to the debtor if he has not signed after default a statement renouncing or modifying his rights under this subdivision. In the case of consumer goods no other notice need be given. In other cases notice shall be sent to any other secured party from whom the secured party has received (before sending his notice to the debtor or before the debtor's renunciation of his rights) written notice of a claim of an interest in the collateral. If the secured party receives objection in writing from a person entitled to receive notification within 21 days after the notice was sent, the secured party must dispose of the collateral under Section 9-504. In the absence of such written objection the secured party may retain the collateral in satisfaction of the debtor's obligation. (Emphasis added.)

Cal. Com. Code Section 9505(2) (West 1990) (identical to U.C.C. Section 9-505(2)) (section references hereinafter are to the Uniform Commercial Code (the "UCC" or "Code"), upon which the California Commercial Code is adopted, unless otherwise indicated).

Section 9-505(2) requires (i) a default, (ii) the secured party to be in possession of the collateral, (iii) the secured

party to send the debtor, and in some cases any other secured party, a written notice that it proposes to retain the collateral in full satisfaction of the debt, and (iv) that the debtor or any party entitled to notice of the proposal must be given twenty-one days after the proposal to object. If all requirements are met and no timely objection is made, then the secured party may retain possession of the collateral in full satisfaction of the debt, and the debtor loses any equity it may have in the collateral. If the secured party is not in possession or fails to give the required notice of proposal to the debtor, or if a party entitled to notice objects, then the secured party must sell the collateral in a commercially reasonable manner pursuant to Section 9-504 and remit any proceeds in excess of the debt to the debtor. The requirements and rights granted under the section cannot be waived prior to default.

This case involves precisely the type of harm that the UCC and the courts have historically striven to prevent: To secure a loan of only $350,000, Hafif took as collateral Debtor's 2 Points, a general intangible, which the Bankruptcy Court found to be worth $1.4 million at the time of Hafif's purported strict foreclosure.

Hafif attempted to have Debtor waive his rights in the Note, a waiver that the law does not permit. Upon default, Hafif did not either judicially or non-judicially foreclose upon the collateral but rather claimed to have obtained title to it by virtue of the legally ineffective waivers in the Note — notwithstanding the fact that Debtor had equity in the collateral in excess of $1,000,000.

It was only after Hafif was sued by Debtor to recover damages for his violation of Article 9 of the California Commercial Code that Hafif claimed that it had really attempted a strict foreclosure of that collateral pursuant to Section 9-505(2). This claim is without merit because the 2 Points, which are general intangible by definition cannot

be possessed for the purpose of a "strict foreclosure" under Section 9-505(2). Even if a strict foreclosure of a general intangible were possible, Hafif completely circumvented the absolutely essential protections provided by Section 9-505(2) by failing to actually propose a strict foreclosure in writing and instead simply stating that the foreclosure was final, without providing Debtor with his statutory opportunity to object.

It is worth noting that, rather than foreclosing upon the 2 Points pursuant to Section 9-504 and remitting the excess proceeds to Debtor, as required under that section, after Hafif received Debtor's objection, Hafif's employee wrote back to inform Debtor that Hafif was "a little bit furious" that Debtor had objected, that Hafif owned the 2 Points, and that if Debtor wanted the 2 Points he would have to purchase them at a premium. In essence, Hafif attempted to unlawfully coerce Debtor into relinquishing all of his interest in the 2 Points, worth $1.4 million, in full satisfaction of a loan of $350,000.

Although the lower courts, and the Ninth Circuit by its affirmance, ruled that Hafif could and did properly foreclose on the 2 Points, these rulings were clearly contrary to the law, violating the default provisions of Article 9 of the Uniform Commercial Code.

A. Sections Of The Code That Require The Secured Party To Be In Possession Do Not Apply To General Intangibles:

Both of the lower courts and the Ninth Circuit recognized that a formal requisite of "strict foreclosure" under Section 9-505(2) is that the secured party must be in "possession" of the collateral. (Judgment, Appendix at 5a; Order, Appendix at 15a-16a; memorandum, Appendix at 23a-24a). In contrast, Section 9-504, which governs foreclosure sales, has no possession requirement, and the secured party may

therefore sell collateral it cannot possess pursuant to Section 9-504.

Section 9-505(2) is not available to Hafif in this case as its collateral is a general intangible that is not capable of being possessed as required by the section. As described in the Note, the collateral is an undivided beneficial interest in a trust and falls within the definition of a "general intangible" under Section 9-106. Section 9-106 defines general intangibles as: "... any personal property (including things in action) other than goods, accounts, chattel paper, documents, instruments, and money." The Bankruptcy Court expressly agreed that the "interest in the trust is a general intangible and ... that a general intangible cannot be possessed in the usual sense." (Judgment, Appendix at 5a). However, the Bankruptcy Court held that: "... while the Plan may not have had actual possession of the collateral, it had sufficient dominion and control over it to constitute possession, for purposes of this section." (Judgment, Appendix at 6a). The District Court and the Ninth Circuit adopted this holding, with the District Court actually contending that nothing in the Code or its comments expressly precluded applying Section 9-505(2) to general intangibles. (Order, Appendix at 16a).

This holding is contrary to the law. The Official Comments to the UCC expressly state that by definition a general intangible cannot be "possessed." For example, the UCC Official Reasons For 1977 Changes to Section 9-305 states that an uncertificated security, which is a general intangible under Section 9-106: "... by definition, cannot be 'possessed.' " Thus, the drafters of the UCC have made clear that a general intangible is an interest that is not capable of being possessed.

More importantly, the drafters designed the Code such that provisions that applied only to secured parties in possession would not apply to general intangibles. Thus, none of

the sections in Article 9 requiring the secured party to be in possession, e.g., sections 9-203, 9-207, 9-305 and 9-503, would apply to property that could not be possessed (such as accounts receivable and general intangibles). The Code has always distinguished between so-called "possessory" and "nonpossessory" security interests.

One example is Section 9-203(1)(a), which is the statute of frauds section of Article 9. Section 9-203(1)(a) provides that "a security interest is not enforceable against the debtor or third parties with respect to the collateral . . . unless . . . (a) the collateral is in the possession of the secured party pursuant to agreement, or the debtor has signed a security agreement which contains a description of the collateral . . .

With regard to this statute of frauds section which distinguishes between possessory and non-possessory security interests, Official Comment 3 to Section 9-203 states:

> One purpose of the formal requisites stated in subsection (1)(a) is evidentiary . . . Where the collateral is in the possession of the secured party, the evidentiary need for a written record is much less than where the collateral is in the debtor's possession; customarily, of course, as a matter of business practice the written record will be kept, but, in this Article as at common law, the writing is not a formal requisite. Subsection (1)(a), therefore, dispenses with the written agreement — and thus with signature and description if the collateral is in the secured party's possession.

Another example is Section 9-305 which sets forth the types of property in which a security interest may be perfected by the secured party's possession. Official Comment 1 to Section 9-305 makes clear that the section does not apply to property that could not be possessed:

> This Section permits a security interest to be perfected by transfer of possession only when the collateral is

> goods, instruments (other than certificated securities, which are governed by Section 8-321), documents or chattel paper: that is to say, *accounts and general intangibles are excluded*... A security interest in accounts and general intangibles — property not ordinarily represented by any writing whose delivery operates to transfer the claim — may under this Article be perfected only by filing, and this rule would not be affected by the fact that a security agreement or other writing described the assignment of such collateral as a "pledge." (Emphasis added.)

Further, Official Comment 5 to Section 9-302, which sets forth when filing is required to perfect a security interest, states:

> This Article adopts the filing requirement [for accounts receivable], on the theory that there is no valid reason why public notice is less appropriate for assignments of accounts than for *any other type of nonpossessory interest.* Section 9-305, furthermore, excludes accounts from the types of collateral which may be the subject of a possessory security interest: filing is thus the only means of perfection contemplated by this Article. (Emphasis added.)

The possession requirement with respect to perfection under Section 9-305, which does not apply to general intangibles, is analogous to the possession requirement of Section 9-505(2). As will be discussed in more detail below, the possession requirement in both sections serves to notify third parties of the secured creditor's interest in the property. Just as perfection by "possession" of a general intangible is not possible under Section 9-305, strict foreclosure of a general intangible is not possible under Section 9-505(2). For example, a general intangible such as goodwill in a company could not be possessed for purposes of perfection or strict foreclosure, and thus perfection by possession and

strict foreclosure cannot be available options. Rather, a secured party would have to file pursuant to Section 9-302 in order to perfect its interest in the general intangible and could only foreclose by selling the general intangible pursuant to Section 9-504.

It is also important to note that this result is unchanged simply because, as the Official Comment to Section 9-305 confirms, a description of the general intangible can be reduced to writing or some permanent form. *See, e.g., In the Matter of Information Exchange, Inc.*, 98 Bankr. 603 (Bankr. N.D. Ga. 1989) (possession of computer tapes was insufficient to perfect a security interest in a computer program (a general intangible), as the tapes did not provide adequate notice to third parties of the secured party's interest in the program).

In their decisions, both the lower courts and the Ninth Circuit failed to recognize that Section 9-305 does not apply to property that cannot be possessed, and blurred the fundamental distinction between sections that require the secured party to be in possession and those that do not. The District Court contented itself with observing that the comments to that Code section state that a security interest in a general intangible can only be perfected by a writing and, here, the trustee of the Marriner Note Trust had written Hafif *prior* to the default to acknowledge: "that Debtor had 'transferred an interest' in the trust and [the trustee] agreed to 'act in accordance with writings from [Hafif] regarding disposition of said two percent undivided beneficial interests.' " (Order, Appendix at 16a). Thus, the courts below missed the point of these sections of the UCC entirely.

For their part, the Bankruptcy Court and the Ninth Circuit relied on *Kruse, Kruse & Miklosko, Inc. v. Beedy*, 353 N.E.2d 514, 20 UCC Reporting Service 217 (Ind. 1976), for the authority that a secured party takes possession of collateral for the purposes of strict foreclosure by

notifying the bailee holding the collateral of the secured party's interest. *Kruse* involved a pledge of capital stock of a corporation which was in the possession of the bailee, and the court in *Kruse* relied on the definition of possession as applied to perfection of security interests under Indiana Commercial Code Section 26-1-9-305, which is the equivalent of UCC Section 9-305. The court in *Kruse* properly applied the section to capital stock, which is not a general intangible but instead an "instrument" as defined in Section 9-105(1)(i) that is capable of being possessed and was in fact possessed by the bailee.

However, by relying on the analysis in *Kruse,* the Bankruptcy Court and the Ninth Circuit were, in effect, applying Section 9-305 to a general intangible, despite the fact that, as discussed above, Section 9-305 does not apply to general intangibles. *Kruse* and Section 9-305 are not applicable to general intangibles, and their reliance on *Kruse* as authority for its decision was misplaced.

The importance of the distinction between possessory and non-possessory security interests was also demonstrated by the Code draftsmen who determined, at the time they formulated the 1977 revisions to the Code dealing with "uncertificated" securities, that certain provisions of a section of Article 9 that apply only in situations where the secured party is in possession could, by means of a drafting technique in a new provision in Article 8, make the Article 9 provisions applicable to "nonpossessory" and "non-possessed" interests dealt with in the new provision in Article 8. To elaborate: the Official Text of the UCC was amended in 1977 to put into Article 8 those provisions, formerly in Article 9, that govern the creation and perfection of security interests in both certificated (i.e., stock) and uncertificated (i.e., "book entry") securities. At the same time, a provision in Article 9, Section 9-207, which sets forth the rights and obligations of a secured party *in possession* of collateral,

was, by virtue of new Section 8-321(3)(b), expressly made applicable to securities now governed by Article 8, thereby avoiding the necessity of repeating the provisions of Section 9-207 in Article 8. Section 8-321(3)(b) states, in part:

> The secured party has the rights and duties provided under Section 9-207, to the extent they are applicable, whether or not the security is certificated, and if certificated, whether or not it is in his possession.

The language in Section 8-321 expressly distinguishes between uncertificated securities (which are general intangibles under Section 9-106) and certificated securities — in order to specifically include both "nonpossessory" uncertificated securities and "non-possessed" certificated securities within the scope of Section 9-207. Section 9-207 otherwise only applies to property in possession of the secured party, and without this express language in Section 8-321, Section 9-207 would not be deemed to apply to uncertificated securities. Section 8-321 likewise expressly "deemed" Section 9-207 to include certificated securities *not in possession*, which also would otherwise not be included in the section. Given this explicit language in Article 8 to expand the scope of Section 9-207 to include certain general intangibles, the drafters of the UCC were indeed demonstrating that without such additional language, general intangibles would not be covered by that section or any other section that requires possession.

Of further significance is the lack of any reference in Section 8-321 to Section 9-505(2). The drafters did not extend the scope of Section 9-505(2) to include general intangibles such as uncertificated securities, even though they clearly understood the necessity of doing so in the context of Section 9-207. Thus, neither general intangibles consisting of book entry securities nor certificated securities not in the secured party's possession are subject to strict foreclosure under Section 9-505(2). The same result neces-

sarily follows with respect to a general intangible consisting of a beneficial interest in a trust, as is involved in this case.

Apparently, the drafters of the UCC are not the only ones who understand that a section that requires the secured party to be in possession of its collateral does not apply when the collateral is not capable of being possessed, such as a general intangible. Although the Uniform Commercial Code has been in effect for several decades now, and Section 9-505 was adopted by California effective January 1, 1976, there is no reported case in which a *secured party* has even attempted a strict foreclosure of an intangible under Section 9-505(2) — or under any comparable statutory or common law provision — let alone a case in which such a strict foreclosure was held to be possible.

In *In re Emergency Beacon,* 48 Bankr. 341 (S.D.N.Y. 1985), relied upon in the District Court's Order, the debtor (*not* the secured party) claimed that the secured party had strictly foreclosed on accounts receivable and hence that the debt should be deemed satisfied under Section 9-505(2). The court's opinion was completely silent, though, as to the issue of whether section 9-505(2) applied to accounts receivable as the court held that the secured party never gave notice to the debtor that it proposed to accept the accounts in full satisfaction of the debtor's obligation. *Id.* at 347.

Although not specifically cited in the Memorandum, *Emergency Beacon* was argued in Hafif's Briefs and the District Court had found this case to be of great significance in supporting its conclusion that a secured creditor could strictly foreclose on a general intangible but this was based on its erroneous belief that an account receivable was a general intangible. In point of fact, Section 9-106 expressly excludes accounts from the definition of a general intangible and the court in *Emergency Beacon* therefore did not address the question whether an intangible could be possessed for purposes of Section 9-505(2). 48 B.R. at 344. That court

did observe, however, that Section 9-505(2) could not be satisfied because the secured lender had never given written notice to the debtor. *Id.* at 347. This holding is readily understandable as the collection of accounts is governed by Section 9-502, not the strict foreclosure provisions of Section 9-505.

B. The Possession Requirement Is An Essential Element Of Strict Foreclosure And Should Not Be Read Out Of The Statute:

The possession requirement in Section 9-505(2) has its basis in the common law preceding the UCC and serves an essential function. Under the common law, possession of the collateral by the secured party was necessary to notify third parties that the debtor was in default and that the secured party had assumed ownership of the collateral. *See. e.g., Stanley v. The Citizens Coal And Coke Co.*, 24 Colo. 103, 49 P. 35 (1897); *Shannon v. Wolf*, 173 Ill. 253, 50 N.E. 682 (1898). Without possession by the secured party or a foreclosure sale, third parties could not know that the debtor no longer had an interest in the property and that the secured party was the owner. In a strict foreclosure, the secured party *retains* the collateral and would generally not have to seek additional court approval in order to enforce its right to possess, use or dispose of the collateral. The secured party's actual and permanent possession served to notify third parties that ownership had indeed changed hands.

No attempt to "possess" a general intangible can meet this essential element of strict foreclosure. Not only can a general intangible not be possessed in any physical sense as conceded by the Bankruptcy Court (*see* Judgment, Appendix at 5a) *and* by the Ninth Circuit, but it also cannot be "possessed" in any manner sufficient to serve the world with notice of the change of ownership. As set forth in Sections 9-302 and 9-305 and the Official Comments to the

UCC, in order to perfect a security interest in a general intangible, nothing short of filing a financing statement with the appropriate authorities is sufficient to notify the world that the secured party has acquired an interest in the general intangible. Likewise, no efforts to "possess" a general intangible — not writing a letter, notifying a trustee of a claimed interest (such as Hafif did as evidenced by the October 11, 1984 letter from the employee of the trustee of the Marriner Note Trust) or holding a document describing the interest — is sufficient to constitute "possession" as required to notify the world that a strict foreclosure has occurred and that ownership has changed.

The lower courts and the Ninth Circuit failed to address this critical purpose behind the possession requirement of Section 9-505(2) when they ruled that "dominion and control" over a general intangible was sufficient. (*See* Judgment, Appendix at 6a; Order, Appendix at 16a). In effect, the courts read the possession requirement out of the statute or waived its application with respect to a general intangible. This is not permissible.

Just as such a reading is implausible with respect to perfection by possession, this interpretation of the possession requirement is implausible with respect to a strict foreclosure. Section 9-505(2) expressly requires a secured party to be in possession of the collateral and cannot apply when the collateral is not, or cannot be, possessed. *See McIlroy Bank & Trust v. Seven Day Builders of Arkansas, Inc.* 1 Ark.App. 121, 132-33; 613 S.W.2d 837, 842 (Ark. Ct. App. 1981) (noting that there could not be a strict foreclosure if the secured party was not in possession of the collateral at the time the letter purportedly electing that remedy was sent).

C. The Harshness Of Strict Foreclosure As A Remedy Mandates That Section 9-505 Should Not Be Expanded Beyond Its Express Language:

Historical accounts of mortgage foreclosures of personal property describe strict foreclosure as having once been the natural remedy in the event of a default. *See* II Grant Gilmore, *Security Interests in Personal Property* Section 43.2 (1965). This flowed from the view that the conveyance of a mortgage vested title in the mortgagee, and foreclosure was akin to an action to quiet title. *See Warner Bros. Co. v. Tiny Freud*, 138 Cal. 651, 72 P. 345 (Cal. 1903). As such, the mortgagor would forfeit title and any interest in the property upon strict foreclosure. Because of the inherent harshness of strict foreclosure to the mortgagor, by the first half of the nineteenth century the practice of strict foreclosure nearly disappeared. *See* II Gilmore Section 43.2. The courts adopted the view that a mortgage represented a mere security for the debt and did not vest title in the mortgagee, and in this manner the mortgagor was entitled to any proceeds from the sale of the land that exceeded the amount of the debt. *See id.; Warner Bros.*, 138 Cal. at 651.

California did not allow strict foreclosure of mortgages on land under any circumstances. *See* John Hanna, *Cases and Other Materials on Security* 864 (1932). Likewise, a provision in a chattel mortgage granting the mortgagee the right to take possession of the chattel upon default and retain the property in satisfaction of the debt was deemed void in California. *Wakabayashi v. Stafford Packing Co.*, 186 Cal. 632, 200 P. 392 (Cal. 1921). While a few states allowed some form of strict foreclosure before the adoption of the UCC, they were in the distinct minority. *See* II Gilmore Section 43.2. Thus, the enactment of Section 9-505(2) in the California Commercial Code created a new,

but limited, strict foreclosure remedy for secured parties that was not theretofore available.

Under the UCC, strict foreclosure continues to be a harsh remedy. Unlike a foreclosure sale under Section 9-504, if the secured creditor complies with Section 9-505(2), the debtor is not entitled to recover any proceeds in excess of the debt, and a strict foreclosure has no counterpart to the commercial reasonableness requirement that exists in the case of a foreclosure sale. The remedy of strict foreclosure is available under Section 9-505(2) because in certain circumstances *both* parties may decide that they are better off if the secured party retains the collateral in exchange for relieving the debtor from any further obligation on the debt. *See* U.C.C. Section 9-505 Comment 1 (West 1990). However, because of the inherent harshness of strict foreclosure should the debtor have equity in the property, the protections afforded the debtor in terms of entitlement to a notice that the secured party proposes to retain the collateral under Section 9-505(2) and the opportunity to object are essential to counterbalance these harsh effects.

The harshness of the remedy of strict foreclosure is readily apparent in the case at hand. Were Section 9-505(2) applicable to general intangibles, Debtor would lose the benefit of a foreclosure sale executed in a commercially reasonable manner pursuant to Section 9-504 and forfeit any proceeds that could have been obtained in excess of the amount of the debt. The Bankruptcy Court acknowledged the validity of the testimony presented by Debtor regarding the value of the 2 Points and that they had considerable value in excess of the amount of the debt. (Judgment, Appendix at 8a). The difference between the value of the 2 Points and the amount due on the note exceeded $1 million, and this loss does not include the interest Debtor would have earned on the excess proceeds that would have been

remitted to him had Hafif bothered to comply with the provisions of the Uniform Commercial Code.

The UCC severely limits the application of strict foreclosure for the very purpose of avoiding the type of harm that occurred in this case. Section 9-505(2) provides that the secured party may only propose a strict foreclosure and give the debtor twenty-one days within which to object. If the debtor objects, then the secured party *must* proceed by means of a foreclosure sale pursuant to Section 9-504. Thus, the debtor has absolute veto power with respect to a strict foreclosure.

The Bankruptcy Court, by holding that Section 9-505(2) applies to collateral that cannot be possessed, expanded the scope of the section beyond its language and intent. The District Court and the Ninth Circuit have ratified this view, albeit in unpublished decisions. Given the harshness of strict foreclosure, the severe limitations on strict foreclosure in the UCC and the historical distaste courts have had for this remedy, the scope of strict foreclosure should not be expanded beyond the Code's express language and intent, especially when the debtor will forfeit a substantial interest in the collateral.

III.

CONCLUSION

For the foregoing reasons, this Court should issue a Writ of Certiorari to review the Judgment of the United States Court of Appeal for the Ninth Circuit.

Dated: June 8, 1994

BUCHALTER, NEMER, FIELDS & YOUNGER
A Professional Corporation

By: JACK I. SAMET
MARVIN D. HEILESON
Attorneys for Petitioner
John Martin-Musumeci

APPENDIX

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

Case No.: 4-89-01694 N3
Adversary Nos.: 4-90-0247 AN, 4-90-0241 AT

IN RE JOHN MARTIN-MUSUMECI,
Debtor.

JOHN MARTIN-MUSUMECI,
Plaintiff,

v.

HERBERT HAFIF,
Defendant.

Oakland, California
August 30, 1991
3:06 p.m.

TELEPHONE CONFERENCE

TRANSCRIPT OF PROCEEDINGS
BEFORE THE
HONORABLE RANDALL J. NEWSOME,
UNITED STATES BANKRUPTCY JUDGE.

APPEARANCE:

For the Plaintiff:	EDWARD MENDOZA GENDEL, RASKOFF, SHAPIRO & QUITTNER 1801 Century Park East, 6th Floor Los Angeles, CA 90067
For the Defendant:	GREG HAFIF LAW OFFICES OF HERBERT HAFIF 269 West Bonita Avenue Claremont, CA 91711-4784 (714) 624-1671
Court Recorder:	CLAIRE S. TESHIMA U.S. Bankruptcy Court 1300 Clay Street Oakland, CA 94612 (415) 273-7212
Transcription Service:	KATHLEEN M. REHLING 613-B Wescoat Court Mountain View, CA 94043 (415) 967-1787

Proceedings recorded by electronic sound recording; transcript produced by transaction service.

OAKLAND, CALIFORNIA,
AUGUST 30, 1991, 3:06 P.M.

THE COURT: Hello?

MR. HAFIF: Hello.

MR. MENDOZA: Hello.

THE COURT: Okay. Gentlemen, would you like to identify yourselves, please?

MR. HAFIF: Greg Hafif for the defendant.

MR. MENDOZA: This is Ed Mendoza for John Martin-Musumeci.

THE COURT: Okay. Gentlemen, I'm going to read my decision into the record. I think this is a more expeditious way of doing things than, as I indicated to you at the trial, than trying to send out a written decision. But, obviously, this can be transcribed. And so I'll start.

MR. HAFIF: Thank you.

THE COURT: These adversary proceedings are before the Court pursuant to a trial on the merits held on August the 26th, 1991. As developed at that trial, a number of areas of disagreement exist between the parties, all having to do with a total of four and a half points in the assets held by Micro/Vest as trustee of the Marriner Note Trust.

The first issue concerns a $350,000 loan from the defendant to the debtor, secured by a two percent undivided beneficial interest in the trust. The agreement which the parties signed on July 11, 1984 had a number of co-authors, including the trustee for the defendant, Martin's counsel, Mr. R.M. Bowman, and Martin himself. While not a model of draftsmanship, its key provisions are not ambiguous. It calls for a loan of $350,000 at 16 percent interest, with interest payments of $28,000 in semi-annual installments. The entire principal balance of the loan was to come due on January the 11th, 1985. If the debtor did not pay in full the principal of the loan on that date, then the defendant had a right to convert a portion of the principal into a one-half point beneficial interest.

No schedule is given for principal payments, and no method is given for valuing the one-half beneficial interest. For purposes of this discussion, these flaws in the instrument are irrelevant, since Martin never made any principal payments.

Of prime importance is the alternative remedy provided upon a default in semi-annual interest payments or "to repay the principal when due." In the event the debtor failed to make an interest installment when due, the Plan was entitled to give him 15 days' written demand for payment "or may elect to accelerate payment of the entire balance remaining unpaid." If no payment was made in 15 days, the Plan could sell a portion of the two percent interest to pay off the note. If neither the Plan nor Martin found a buyer within 90 days, then on the 91st day, "full title to said security shall transfer to the holder and shall be deemed full satisfaction of the entire obligation."

Because Martin did not make the January 11th, 1985 interest payment on the note, on March 13th, 1985, the Plan gave Martin his 15-day notice and accelerated the principal balance on the note. While the letter makes reference to the Plan's right of conversion, the reference to the acceleration of the total balance of the principal and of the unpaid interest installment should have put an ordinary, reasonable person on notice that the Plan was opting for its alternative remedy of foreclosure and not the one-half point conversion remedy.

I do not credit Martin's testimony that he reached an oral agreement with Hafif the day after he received the letter, whereby Hafif would only exercise his one-half point conversion right. It is inconceivable to me, especially given the cast of characters and their paper-trail tendencies, that they would leave the disposition of hundreds of thousands of dollars to an oral agreement which was directly contradictory to a written directive.

Despite the fact that Martin completed some $1.4 million in sales of fractional interests in the trust during the week after March 13th, 1985, he never paid a penny on the $350,000 loan. While it is true that the Plan did nothing to line up a buyer, Martin, who now claims that buyers were

readily available — buyers were readily available at the time, did nothing as well, apparently.

On August the 13th, 1985, some 150 or more days after the March 13th notice, the Plan notified Martin that, pursuant to the July 11th, 1984 agreement, title to the note was vested in the Plan. Martin argues that, because the Plan did not follow the dictates of California Commercial Code 9505(2), it did not effectuate a strict foreclosure on the two percent interest securing the note. I disagree, and find that a strict foreclosure was properly effectuated.

Section 9505(2) requires three steps for a strict foreclosure on collateral. One, the secured party must be in possession of the collateral. Two, the secured party must give written notice of its proposal to retain the collateral in satisfaction of the obligation. And, three, the debtor must be given 21 days to object to the foreclosure in writing. See, e.g., *Kruse, Kruse & Miklosko, Inc. v. Beedy*, 20 U.C.C. Reporting Service, 217 at 236, 353 Northeast 2d. 514, 1976, interpreting the 1963 version of the Uniform Commercial Code. See also *White & Summer's Uniform Commerial Code*, 1106, 1978.

Martin asserts that the trust interest is a general intangible, that possession cannot be had of a general intangible, and thus the Plan fails to meet the first requirement of Section 505(2). I agree that the interest in the trust is a general intangible, and would agree that a general intangible cannot be possessed in the usual sense.

Nonetheless, Section 9505(2) does not limit its applicability to certain kinds of collateral. Indeed, the reach of the Commercial Code otherwise extends to both the creation and enforcement of a security interest in general intangibles. It would violate basic principles of statutory construction to read this form of collateral out of Section 9505(2).

Further, I find that while the Plan may not have had actual possession of this collateral, it had sufficient dominion and control over it to constitute "possession" for purposes of this section. While there was no absolute assignment of the two percent, in a letter to Hafif of July 16th, 1984, Micro/Vest itself recognized that Martin had "transferred an interest" in the trust and agreed to "act in accord with writings from your office regarding disposition of said two percent undivided beneficial interest."

This clear acknowledgement by the trustee that the two percent interest was now under the control of a secured creditor is what distinguishes this case from *Sprangers v. Fundamental Business Technology, Inc.*, 4 U.C.C. Rep. Service 2d., 1322, Minnesota Court of Appeals, 1987, a case upon which Martin relies upon, wherein a third party bank refused to give control of the collateral to the creditor — to the creditor. It's also what makes it closer on the facts to *Kruse, Kruse & Miklosko, Inc. v. Beedy*, supra, at 236, where the court held that:

> "Possession of collateral by a bailee who has received notification of the interest of a secured party is considered to be possession by the secured party."

See also *Copeland v. Stewart*, 52 Cal. App. 3rd, 217, 124 Cal. Reporter 860, 867-868, 1975. See also *White & Summer's* at 937.

Martin next asserts that the August 13th, 1985 letter did not "propose" to keep the collateral as required by 9505(2), but instead presented strict foreclosure as an accomplished fact. While the letter does state that the foreclosure is final, "with title vested in the pension plan," the fact remained that, thereafter, Martin did nothing to protect the loss of the two percent. His halfhearted assertion that he felt it was too late is not credible, particularly in light of defendant's August 25th letter which left the door open for Martin to

repurchase the two percent for the principal and interest owing. Had he sent a written objection within the 21-day period prescribed by the statute, he might now be in a position to assert his rights under Section 9504. Having failed to object, he lost that right, and the foreclosure became valid.

Parenthetically, it should be noted that the present version of the statute, unlike the 1963 version of 9505(2), does not require the creditor to inform the debtor of his right to object to the foreclosure. Even if the August 13th, 1985 letter was not in the nature of a proposal, I find that the March 13th, 1985 letter can be fairly read as being one. Consistent with their agreement, Martin was given 90 days to find a buyer of the two percent. During that time, he must surely have been aware of the fact that the Plan was doing nothing to sell the note, and probably intended to keep it. He neither found a buyer, nor paid off the note, nor protested the impending foreclosure called for under the agreement. If the Plan had, in fact, irrevocably foreclosed on the two percent prior to the August 13th letter, it was certainly within its right to do so under Section 9505(2).

Accordingly, I conclude that ownership of the two percent lawfully resides in the Plan pursuant to a properly executed strict foreclosure.

The question of value of the points is now mooted by this conclusion. Nonetheless, I credit the valuation testimony presented by Martin over that presented by the Plan. Points had been sold to an investment banker for some $750,000 each only four months prior to August of 1985. Regardless of whether this price makes sense given the underlying values of Computerland or IMS, it is still the best indicator of fair market value in these circumstances.

Putting aside Hafif's gloomy picture of ComputerLand's future, the fact is that his own pension plan priced these

points in its August 25, 1985 letter at a low of $500,000 in late 1985 to a high of $1.7 million in late 1986. The fact that, subsequent to that time, new light was shed on ComputerLand's fortunes is simply irrelevant.

Accordingly, I find that the points were worth $700,000 on August the 13th, 1985.

The next issue concerns the parties' rights to dividends under the July 11, 1984 loan agreement and the October 10, 1984 agreement to purchase two and a half points for $500,000. The October 10 agreement is quite clear on this point. Martin is entitled to all dividends that accrued prior to October 1, 1984, and the Plan is entitled to all dividends accruing after that date. Martin's uncontroverted testimony is that no dividends accrued after October 1, 1984. Thus, I find he's entitled to all of the dividends derived from that two and a half percent interest.

A significant dispute arose as to the appropriate amount of the dividends to which he is entitled. Without going into great mathematical detail, I find that two and a half percent, rather than the one and a quarter percent asserted by the Plan, is the correct starting point in the calculation, and that 4,331 shares is the most accurate amount for dividends that accrued to Martin.

A contrary conclusion must be reached as to the two percent loan agreement. That agreement says that Martin will retain the right to receive accrued dividends "until such date upon which any portion is sold under foreclosure." Giving the words their plain meaning, this language merely restates a right which is already provided for in Commercial Code 9306. In other words, the right to be paid any proceeds from the collateral would remain with Martin until foreclosure, at which point it would pass to the Plan. If Martin intended to retain the right to receive dividends, he certainly

knew how to say so, as is obvious from the October 10 agreement.

Accordingly, I conclude that the right to be paid any accrued dividends on the two percent passed to the Plan upon foreclosure.

The final issue concerns Martin's right to reimbursement for advances of attorneys' fees paid pursuant to the Marriner Note Trust. Martin admits that he has already received stock from Micro/Vest as reimbursement for these advances. However, he claims that he is entitled to put this stock to the Plan and receive back some $51,744.02 in cash. He admits that neither the two percent loan agreement nor the two and a half percent purchase agreement confer this right on him. The loan agreement merely states that "the legal payment obligations" shall pass to the Plan upon foreclosure. The purchase agreement says that the Plan will be responsible for reimbursement of expenses after October 1, 1984.

Martin asserts that fairness requires that he be allowed to put the stock to the Plan for cash, because the stock he received from Micro/Vest was assigned an agreed-upon value of $17.00 but is now only worth $10.00 to $13.00. No support other than his own testimony is given for these values. Putting that aside, had Hafif been paid in cash as reimbursement for costs he expended in obtaining a verdict in the trust's favor, I might be inclined to agree with Martin. But if fairness is the standard, then I find it only fair that Martin be paid in the same currency as Hafif: Computerland stock.

This conclusion obviates the need for determining the amount of reimbursement Martin actually paid on the four and a half points after they vested in Hafif — in the Plan; excuse me. I would note, however, that Martin's evidence on this point does not meet his burden of proof. Based on the

dates of the checks he submitted, it appears that only $178,920.00 were paid after August the 13th, 1985. .1467 of that amount comes to $26,247.56.

Further, it is not clear whether the post-August the 13th, 1985 payments for fees were for fees that accrued after that date or were simply late payments for fees that accrued pior to that time.

At any rate, I conclude that Martin is not entitled to put any of the stock he received as fee reimbursement to the Plan.

For the reasons stated, judgment will be entered accordingly on the causes of action that have been stated in the complaint. It is so ordered.

Gentlemen, is there anything else? Do you have any questions.

MR. HAFIF: Well, I guess maybe we'll just have to work out how the stock will transfer to Martin versus an appeal, but I guess that'll be between Mr. Mendoza and myself.

THE COURT: Okay.

MR. MENDOZA: Your Honor, one other aspect of this thing is the possibility of future distributions by Micro/Vest. This is a claim for declaratory relief. Can we have a declaration as to future dividend rights on the October 10th agreement?

THE COURT: As stated, my understanding of the October 10th agreement is that there weren't any dividends that accrued prior to — after October 1 of 1984.

MR. MENDOZA: Okay. I understand.

THE COURT: I have no evidence of anything else.

MR. MENDOZA: All right.

THE COURT: Okay?

MR. MENDOZA: Yes.

THE COURT: All right. We'll put on a judgment entry, but as to the findings of fact and conclusions of law, the foregoing constitutes my findings of fact and conclusions of law under Rule 52. And if you want a copy of them, you can order a copy of this transcript. Otherwise, I'm going to put on a judgment entry that's consistent with these findings.

MR. HAFIF: I don't have any problem with that, Your Honor.

THE COURT: Okay.

MR. MENDOZA: All right. Thank you, Your Honor.

THE COURT: Thank you, gentlemen. Bye.

MR. MENDOZA: Good-bye.

(Telephone conference proceedings concluded at approximately 3:21 p.m.)

CERTIFICATE

I certify that the foregoing is a correct transcript from the electronic sound recording of the proceedings in the above-entitled matter.

KATHLEEN M. REHLING _____

Kathleen M. Rehling, Transcriber Date

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA
Case No. C 92-0494 BAC

In re

JOHN MARTIN-MUSUMECI, et al.,

Debtor.

JOHN MARTIN-MUSUMECI, et al.,

Appellant,

vs.

LAW OFFICES OF HERBERT HAFIF PENSION AND PROFIT SHARING PLAN,

Appellee.

ORDER

I. FACTS AND BACKGROUND

On July 11, 1984, Appellee made a loan to the Debtor in the amount of $350,000 at 16% interest, with interest payments of $28,000 in semi-annual installments. The first installment was due on January 11, 1985. Debtor executed a note in favor of Appellee, secured by a two percent interest of the undivided beneficial interest in the Marriner Note Trust (the "Trust"). Debtor was one of the drafters of the loan agreement.

The Note provided that in the event Debtor failed to make any interest installment payments when due, Appellee may, within 90 days of making a written demand for payment, sell the two percent interest in the Trust ("2 Points"). The Note also provided that if the 2 Points were not sold within the 90 day period, then ". . . full title to said security shall transfer to the Holder [Appellee] and shall be deemed full satisfaction of the entire obligation; I

[Debtor] shall not be liable for any real or alleged deficiency." As an alternative remedy, the Note provided that the Appellee had the right to convert one-half of one percent of the interest in the Trust as repayment.

Because Debtor failed to make the Jan. 11, 1985 interest payment on the note, by letter dated March 13th, 1985, pursuant to the terms and conditions of the Note, Appellee gave Debtor 15-day notice and accelerated the principal balance on the note. The letter referred to Appellee's right to conversion; however, the letter specifically stated that Appellee would not exercise that right. The Bankruptcy court held that the letter should have put Appellant on notice that Appellee was opting for the foreclosure option.

Debtor failed to respond to the March 13th letter. On August 13, 1985, five months later, Appellee sent Debtor another letter stating that pursuant to the terms of the agreement, Appellee had foreclosed on the Note. The letter specifically noted that Debtor's involvement in litigation precluded Appellee from selling the security because it would expose the plan participants to liability. As Debtor had failed to secure a buyer, Appellee was forced to foreclose. The letter specifically left open the possibility of Debtor's repurchasing the securities from Appellee.

On August 25, 1985 Appellee sent another letter to Debtor again offering Debtor an out. While expressly stating that Appellee owned the 2 Points, the letter gave Debtor an additional 60 days to buy back the 2 Points for the principal and interest due to date. The letter made further provisions for buying back the 2 Points at later dates for higher prices. Debtor failed to respond to this last offer.

Appellee did not hear from Debtor again about the loans until five years later. In 1988 Debtor filed for bankruptcy. In 1990, five years after the foreclosure, Debtor filed suit against Appellee alleging that the foreclosure had violated

Cal. Commerical Code § 9504(3).[1] After a trial before the Bankruptcy Court, the court found that the foreclosure complied with the requirements of § 9595(2).[2]

II. STANDARD OF APPELLATE REVIEW

The Bankruptcy Court's findings of fact are reviewed under the clearly erroneous standard, and the Bankruptcy Court's conclusions of law are reviewed *de novo. See, In the Matter of Pizza of Hawaii, Inc.,* 761 F.2d 1374, 1377 (9th Cir. 1985). Appellant maintains that this appeal concerns solely questions of law. However, Appellee properly argues that the issue of whether or not appellant was given proper notice of Appellee's intent to strictly foreclose is a question of fact which should be reviewed under the clearly erroneous standard. The other issues presented by this appeal are to be reviewed *de novo.*

---

[1]Debtor maintains that Appellee should have foreclosed under Cal. Commercial Code § 9504(3) instead of § 9505(2) because § 9504 does not have a possession requirement.

[2]Section 9505(2) provides that:

> In any other case involving consumer goods or any other collateral *a secured party in possession* may, after default, propose to retain the collateral in satisfaction of the obligation. Written notice of such proposal shall be sent to the debtor if he has not signed after default a statement renouncing or modifying his rights under this subdivision. In the case of consumer goods no other notice need be given. In other cases notice shall be sent to any other secured party from whom the secured party has received (before sending his notice to the debtor or before the debtor's renunciation of his rights) written notice of a claim of an interest in the collateral. If the secured party received abjection in writing from a person entitled to receive notification within 21 days after the notice was sent, the secured party must dispose of the collateral under Section 9504. In the absence of such written objection the secured party may retain the collateral in satisfaction of the debtor's obligation. (Emphasis added.)

III. DISCUSSION

Under § 9505(2), the secured party has available to it the remedy of "strict foreclosure" in the event Debtor fails to make payments on the debt. "Strict foreclosure" allows the secured party to retain the collateral in full satisfaction of the debt. Section 9505(2) requires: (i) a default, (ii) the secured party to be in possession of the collateral, (iii) in cases not involving consumer goods, the secured party must send written notice to the debtor (in some cases other secured parties) that it proposes to retain the collateral in full satisfaction of the debt, and (iv) that the debtor or any other party entitled to notice be given twenty-one days after the proposal to object.

There is no dispute that Debtor defaulted. Debtor, however, seeks to overturn the bankruptcy court's ruling on two grounds. First, Debtor maintains that as the two percent interest in the trust fund is a general intangible asset which cannot be possessed, § 9505 does not apply. Second, assuming that § 9505(2) applies, Debtor argues that the bankruptcy court erred in finding that Appellee gave Debtor written notice of foreclosure as required by § 9505(2)

A. Possession of Collateral

Debtor maintains that as the trust property is a general intangible, Appellee could not have possession over it as required before § 9505(2) applies. This argument must fail for two reasons, both articulated by the bankruptcy court. First, § 9505(2) does not limit its application to certain kinds of collateral. There is nothing in either §§ 9505(2) or 9504, or the comments to those sections, which specifically limits the application of § 9505(2) as Debtor suggests.

Debtor argues that by definition, Appellee cannot be in possession of a general intangible as defined in § 9-106 of the U.C.C. Debtor cites to the comments of U.C.C. § 9-305 for this proposition. However, the comments to that section

only state that a security interest in a general intangible, ordinarily not represented by a writing, can only be perfected by a writing. (Comment 1). Debtor cites to no authority which states that a secured creditor of a general intangible interest cannot avail itself of the rights contained in § 9505(2).

Second, the bankruptcy judge found that while Appellee may not have been in actual possession of the collateral, it had sufficient dominion and control over it to constitute "possession" for purposes of § 9505(2). This holding was based on a finding that the trustee to the trust acknowledged Appellee's control over the two percent interest in a letter to Appellee dated July 16, 1984, in which the trustee recognized that Debtor had "transferred an interest" in the trust and agreed to "act in accordance with writings from your office regarding disposition of said two percent undivided beneficial interests."

The Law of Secured Transactions Under the Uniform Commercial Code, 2d Ed., Section 4.10[3], pp. 159-160, states:

> "For another case that implies that retention and satisfaction of the debt is permissible even when the collateral is intangible, such as accounts receivable, see *In re Emergency Beacon Corp.* The clear implication from the case is that strict foreclosure would be available as an option for the accounts assignee."

In *In re Emergency Beacon Corp.*, 441 U.C.C. Rep. 1544 (JD N.Y. 1985), 48 B.R. 341, the Debtor received a loan from the Creditor that was secured in part by Debtor's accounts receivable, a general intangible. To satisfy the debt, Debtor turned over to Creditor its accounts receivable. The court specifically held that Creditor acquired possession of the accounts receivable. *Id.* at 346. Here Debtor attempts to distinguish *In re Emergency Beacon Corp.* by arguing that

the court did not address the question of whether an intangible could be possessed for purposes of § 9505(2). However, the primary importance of *In re Emergency Beacon Corp.* is its holding that a secured creditor can strictly foreclose on a general intangible.

Once it is determined that Appellee had sufficient possession of the collateral for purposes of § 9505(2), it must be determined whether Appellee gave Debtor sufficient notice.

B. Sufficiency of Notice

Debtor argues that he was never given notice of Appellee's intention to exercise the "strict foreclosure" option. Debtor argues that the August 13, 1985 letter did not "propose" to keep the collateral as required by §9505(2). Instead, the letter indicated that Appellee had already foreclosed, and thus made objection fruitless. The bankruptcy court found, first, that Debtor's assertions that he could not object were not credible, especially in light of the August 25 letter which specifically gave him a right to pay off the note. Second, the court found that the March 13th letter was sufficient notice of a proposal to foreclose.

The bankruptcy court's finding on the notice issue presents questions of fact which are reviewed under the clearly erroneous standard. Here, the March 13th letter clearly gave notice that Debtor was in default. Additionally, as the bankruptcy court found, the letter indicated that Appellee did not wish to exercise its right to conversion. The court found that this letter was sufficient notice. The fact that Debtor did nothing to address this issue, despite repeated requests, further supports the bankruptcy court's findings.

CONCLUSION

For the foregoing reasons, the bankruptcy court's order is AFFIRMED.

IT IS SO ORDERED.

Date: 7/30/92

BARBARA A. CAULFIELD

BARBARA A. CAULFIELD
United States District Judge

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

No. 92-16528

D.C. No. C-92-494-BAC

Bankr. No. 4-89-01694 N3
(Chapter 11)

In re

JOHN MARTIN-MUSUMECI, etc.,

Debtor.

JOHN MARTIN-MUSUMECI, etc.,

Plaintiff-Appellant,

v.

LAW OFFICES OF HERBERT HAFIF
PENSION AND PROFIT SHARING PLAN,

Defendant-Appellee.

MEMORANDUM*

Appeal from the United States District Court
For the Northern District of California
Barbara A. Caulfield, District Judge, Presiding

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*This disposition is not appropriate for publication and may not be cited to or by the courts of this circuit except as provided by Ninth Cir. R. 36-3.

Argued and submitted January 13, 1994
San Francisco, California

BEFORE: SCHROEDER, NOONAN, Circuit Judges, and JONES,** District Judge

INTRODUCTION

Appellant, a Chapter 11 debtor, alleges that his attorney's pension plan, which loaned appellant money, did not have the right to strictly foreclose on the two percent interest in a trust the plan held as security for the loan. Appellant alleges that the plan was incapable of possessing the trust interest, a general intangible, and as such could not effect a strict foreclosure.

Although as a rule a general intangible such as a trust interest cannot be possessed, we affirm the district court because based on this unique set of facts we find the plan was in possession of the collateral and could strictly foreclose when appellant defaulted.

FACTS AND PROCEEDINGS

The loan at the heart of this case was made on July 11, 1984 by attorney Herbert Hafif to his then-client, John Martin-Musumeci ("debtor"), who eventually filed for bankruptcy. The $350,000 loan came from funds held by the Herbert Hafif Pension and Profit Sharing Plan ("the plan").

Debtor executed a note in favor of the plan secured by a two percent interest of the undivided beneficial interest in the Marriner Note Trust ("the trust"), also known as the Micro/Vest trust. According to appellee, Micro/Vest was a corporation with assets of a single note which on its face

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**The Honorable Robert E. Jones, United States District Judge, District of Oregon, sitting by designation.

gave the holder the right to convert the outstanding balance of the note into 20 percent of the shares of Computerland stock. The note executed by debtor (not to be confused with the note Micro/Vest owned) provided that in the event debtor failed to make any interest installment payments when due, the plan may, within 90 days of making a written demand for payment, sell the two percent interest in the trust ("the two points"). The note also provided that if the two points were not sold within the 90 days period, then:

> full title to said security shall transfer to the holder [the plan] and shall be deemed full satisfaction of the entire obligation; I [debtor] shall not be liable for any real or alleged deficiency.

The note provided that Hafif had the right to convert one-half of one percent of the interest in the trust as repayment as an alternate remedy.

Debtor failed to make the January 11, 1985 interest payment. By letter dated March 13, 1985, Hafif's office, on behalf of the plan, gave debtor 15 days' notice and accelerated the principal balance on the note. This notice letter also said, "We certainly do not wish to exercise our right of conversion." When debtor failed to respond, Hafif's office sent debtor another letter dated August 13, 1985, stating that pursuant to the terms of the agreement, the plan had foreclosed on the note. This letter noted:

> [T]his is not a security we can sell. This is especially true in light of the lawsuits against Microvest [sic]. We can not subject the pension plan participants to exposure to multi-million dollar lawsuits over the sale of the security.
>
> Furthermore, since your efforts to sell the security have been unavailing, efforts which we appreciate have been made more difficult by the lawsuits, and since we owe

> the utmost fiduciary duty to our plan's participants, the plan has foreclosed on the security.

Hafif's office also told debtor that should he wish to repurchase the two points, the plan would "seriously consider any good faith, reasonable and fair offer."

Debtor received a third letter from the plan on August 25, 1985 notifying him that, while the plan was now the full owner of the two points, he had an additional 60 days to buy back any portion of the two points for the principal amount. The letter contained additional provisions for buying back the two points later for more money. Debtor did not respond to this last offer.

Three years later debtor filed for bankruptcy. In 1990, five years after the plan had foreclosed on the two points, debtor filed suit in bankruptcy court against the plan alleging that the foreclosure violated California Commercial Code Section 9-504(3), which covers the sale of collateral after a default. Following trial, the bankruptcy court found that the plan had complied with the provisions of California Commercial Code Section 9-505(2), which provides that a secured party in possession can strictly foreclose if notice has been given and there is no objection within a 21-day period.[1]

---

[1]This section reads:

> In any case involving consumer goods or any other collateral a secured party in possession may, after default propose to retain the collateral in satisfaction of the obligation. Written notice of such proposal shall be sent to the debtor if he has not signed after default a statement renouncing or modifying his rights under this subdivision. In the case of consumer goods no other notice need be given. In other cases notice shall be sent to any other secured party from whom the secured party has received (before sending his notice to the debtor or before the debtor's renunciation of his rights) written notice of a claim of an interest in the collateral. If the secured party receives objection in writing from a person entitled to receive notification within 21 days after the notice was sent, the secured party must dispose of the collateral under Section 9504. In the

Debtor unsuccessfully moved to alter judgment and then appealed to the district court, which affirmed the judgment of the bankruptcy court on July 30, 1992.

STANDARD OF APPELLATE REVIEW

Because this panel is in as good a position as the district court to review the bankruptcy court's findings, we independently review the bankruptcy court's decision. *Matter of Pizza of Hawaii, Inc.*, 761 F.2d 1374, 1377 (9th Cir. 1985). We review the bankruptcy court's findings of fact under the clearly erroneous standard; conclusions of law are reviewed *de novo. Id.*

Whether or not the points were capable of possession and whether the plan did in fact possess them are questions of law we review *de novo.* Whether or not notice was given is a factual determination, *In re Professional Inv. Properties of America*, 955 F.2d 623, 626 (9th Cir. 1992), *cert. denied*, 113 S.Ct. 63 (1992); thus, we review the notice issue for indication that the district court's ruling was clearly erroneous.

DISCUSSION

Section 9-505(2) "presents an uncomplicated blueprint for strict foreclosure on default." 2 White & Summers, *Uniform Commercial Code* 586 (3rd ed. 1988) (hereinafter "White & Summers"). The California code section, like its UCC counterpart, provides the secured party the remedy of strict foreclosure in the event the debtor defaults, a remedy that allows the secured party to retain the collateral in full satisfaction of the debt. In order to meet the requirements of a strict foreclosure under Section 9-505(2), there must be (1) a default; (2) a secured party in possession of the

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absence of such written objection the secured party may retain the collateral in satisfaction of the debtor's obligation.
Cal. Com. Code Section 9-505(2).

collateral; (3) written notice sent to the debtor by the secured party that the secured party proposes to retain the collateral in full satisfaction of the debtor; and (4) a period of 21 days during which time the debtor may object to the proposed retention of the collateral. White & Summers at 586-87.

Because debtor never made any payments on the loan, there is clearly a default. Debtor, then, seeks to overturn the district court's decision on three grounds: (1) the interest in the trust is a general intangible that cannot be possessed and thus Section 9505(2) does not apply; however, if Section 9-505 does apply, (2) the plan did not give adequate notice of its proposal to retain the collateral in satisfaction of the debt as required by Section 9-505(2); and (3) debtor gave proper notice of his objection to the plan's retention of the collateral as required by Section 9-505(2).

1. *Was the trust interest, as a general intangible, incapable of possession?*

Appellant is correct in his assertion that as a general rule, a general intangible cannot be possessed.

> Since the creditor's possession (and the debtor's lack of it) is designed to put third parties on notice, the collateral must be the type that one can see, touch, and move. The collateral must have a physical embodiment recognizable as exclusively representing the right. Thus it follows that accounts and general intangibles cannot be perfected by possession.

White & Summers at 348. No perfection of general intangibles by possession is possible because general intangibles, by their nature, cannot be possessed.

However, under these limited circumstances and only for purposes of Section 9-505 applicability, we find that the plan was in possession of the two points in the trust by virtue of a

letter from the treasurer of Micro/Vest to Hafif as the plan representative. That letter reads, in pertinent part:

> As Treasurer of Micro/Vest Corporation, I am authorized to verify the existence and relative size of various beneficial interests and the identities of the holders. . .
>
> This is to verify and acknowledge that Micro/Vest Corporation, as trutee (sic), has been advised and recognizes that Mr. John Martin-Musumeci has transferred an interest to you equal to two percent (out of 100%) of the full undivided beneficial interest in the trust, which interest is to be held by you as security for a promissory note made by Mr. Martin-Musumeci. I acknowledge that Mr. Martin-Musumeci has the authority and ownership necessary to make such transfer valid. I further agree that this corporation shall act in accord with writings from your office regarding disposition of said 2% undivided beneficial interest.[2]

This letter, dated July 16, 1984, has the effect of giving the plan the status of a secured party in possession of collateral, which in turn qualified the plan to effect a strict foreclosure pursuant to § 9505(2). As one court explained:

> Thus, the possession of collateral by a bailee who has received notification of the interest of a secured party is considered to be possession by the secured party.

Kruse, Kruse & Miklosko v. Beedy, 353 N.E. 2nd 514, 539 (Ind. App. 1976) ("*Kruse*"). This ruling was cited approvingly in 9 Anderson, *Uniform Commercial Code* 801 (3rd ed. 1985):

> A secured party is in possession of the collateral for the purposes of UCC § 9-505 while the collateral is in the

---

[2]The letter also explains that Micro/Vest Corporation is the plaintiff in litigation to enforce conversion of the note into capital stock.

possession of an escrow who knew of the security interest at the inception of the escrow arrangement.

Based on the letter from the Micro/Vest treasurer, who was acting as a bailee and had notice of the plan's interest, we find that the plan was in possession of the two points for purposes of § 9-505(2) and could proceed under that statute.

2. *Did the plan give adequate notice of its proposal to retain the collateral?*

The bankrutpcy court found that the March 13, 1985 letter served as notice that the plan was proposing to keep the collateral in satisfaction of the debt. This letter specifically indicates that the plan is giving "notice pursuant to the terms and conditions of the note." Pursuant to the agreement, debtor was given 90 days to find a buyer for the two percent. The bankruptcy court found that debtor "neither found a buyer, nor paid off the note, nor protested the impending foreclosure called for in the agreement."

The plan again warned debtor about foreclosure in the August 13, 1985 letter and in a third letter dated August 25, 1985. In this latter correspondence, the plan gave debtor 60 days to buy back the two points, which the bankruptcy court found made debtor's assertion that he thought it was too late to object to the foreclosure not credible.

The bankruptcy judge's determination that notice was given was not clearly erroneous. Furthermore, even if we review *de novo* reasonableness of notice as a matter of law, as debtor urges, we find the three letters sent to debtor over a six-month period constituted notice that the plan was proposing strict foreclosure. Although the letters of August 13 and 25 present the forelcosure as a *fait accompli,* both letters also give debtor a repurchase option. In fact, the letter of August 25 gives debtor 60 days to buy back the two points, which exceeds the statutory requirement of 21 days

for the debtor to file objections. Still the plan heard nothing from debtor.

We find that debtor received notice regarding the plan's proposal to strictly foreclose.

3. *Did debtor give proper notice of his objection?*

Debtor maintains that if the literal requirements of "possession" and "written proposal" are to be read out of § 9-505(2), then the court should find that a reference to debtor's objection in Hafif's August 25, 1985 letter "complies with the spirit" of § 9-505(2)'s requirement that objections be filed in writing. This argument is without merit. The statute explicitly requires written objections, which debtor failed to make.

We find debtor failed to give proper notice of his objection.

CONCLUSION

The judgment of the district court is AFFIRMED.

In re John Martin-Musmeci, No. 92-16528

NOONAN, Circuit Judge, dissenting:

As the disposition of the court acknowledges, a general intangible cannot be possessed. As possession was necessary under California law for foreclosure, no foreclosure occurred. I would reverse.

Supreme Court, U.S.
FILED
JUL 0 1994
OFFICE OF THE CLERK

No. 93-1992

In The

Supreme Court of the United States

October Term, 1994

JOHN MARTIN-MUSUMECI, etc.,

Petitioner,

vs.

LAW OFFICES OF HERBERT HAFIF
PENSION AND PROFIT SHARING PLAN,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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STATEMENT OF JURISDICTION

Respondent believes this court lacks jurisdiction and that the case is not, as the Petitioner suggests, as "so far departed from the accepted and usual course of judicial proceedings . . . as to call for and exercise of this court's power and supervision." It is simply a correct, unpublished decision by the Ninth Circuit Court of Appeals, a decision which clearly is within their discretion if not mandated by Rule 36-2, which limits the Ninth Circuit Court of Appeals ability to seek the publication of an opinion. In addition, the area of law requested for review is not "unsettled", but rather well defined.

STATUTES INVOLVED

California *Commercial Code* Section 9505(2):

> "(2) In any other case involving consumer goods or any other collateral a secured party in possession may, after default, propose to retain the collateral in satisfaction of the obligation. Written notice of such proposal shall be sent to the debtor if he has not signed after default a statement renouncing or modifying his rights under this subdivision. In the case of consumer goods no other notice need be given. In other cases notice shall be sent to any other secured party from whom the secured party has received (before sending his notice to the debtor or before the debtor's renunciation of his rights) written notice of a claim of an interest in the collateral. If the secured party receives objection in writing from a person entitled to receive notification within 21 days after the notice was sent,

> the secured party must dispose of the collateral under Section 9504. In the absence of such written objection the secured party may retain the collateral in satisfaction of the debtor's obligation."

STATEMENT OF THE CASE

The undisputed facts reveal that in July of 1984, John Martin (Petitioner), through a series of misrepresentations as to value, induced Respondent to lend him $350,000, upon which loan he has never paid a penny in interest or principal and which Respondent to this day has been unable to sell.

This fraudulently obtained loan was secured by a pledge of "two points" of a beneficial interest in something called Micro/Vest. In essence, it constituted a beneficial interest in a trust.

Micro/Vest was a corporation without directors, shareholders or assets, other than a single note, which on its face provided the holder of the note the right to convert the outstanding balance of the note into 20% of the shares of Computerland stock.

Pursuant to the terms of the note, Petitioner was to make interest only payments every six months. He never made one payment. On March 13, 1985, the Law Offices of Herbert Hafif Pension & Profit Sharing Plan (hereinafter "the Plan") sent Petitioner written notice of default. Still, no payment was ever made. On August 13, 1985, the Plan gave Petitioner written notice of retention and foreclosure. The written notice stated:

> "As has been communicated to you several times, this is not a security we can sell. This is especially true in light of the lawsuits against Micro/Vest. We cannot subject the pension plan participants to exposure to multi-million dollar lawsuits over the sale of the security.
>
> Furthermore, since your efforts to sell the security have been unavailing, efforts which we appreciate have been made more difficult by the lawsuits, and since we owe the utmost fiduciary duty to our plan's participants, the plan has foreclosed on the security.
>
> We deem the foreclosure final with title to the security vested in the pension plan."

No written objection was ever made by the Petitioner to the Plan's retention of the security under California *Commercial Code* Section 9505(2). (Findings, p. 8.)

Approximately three years later in 1988, the Petitioner filed for bankruptcy. In 1990, *five years* after the Plan had foreclosed on the two points, the Petitioner filed suit against Respondent for violation of California *Commercial Code* Section 9504(3).

The Petitioner has alleged that the Respondent did not have the right to strictly foreclose on the two points under California *Commercial Code* Section 9505(2). Petitioner argues that the Plan was required to sell the two points under California *Commercial Code* Section 9504(3) and distribute any excess proceeds to Petitioner.

The Respondent still retains the security, and although the law is abundantly clear that no monetary damages are available to Petitioner when the security has

not been disposed of, it is clear from the testimony provided during trial that the two points were not remotely worth the principal and interest owed by Petitioner.

By Petitioner's own expert testimony, he has "not investigated the market thoroughly" but has placed a value of $700,000 on each point because that "is what people are willing to pay or willing to sell them for . . . " (Transcript, p. 111.)[1] In fact, in 1985, the year of the foreclosure, there were only five transactions that occurred, "three to the Myers group, one to the Griswolds, and the final was to the pension plan." (Findings, p. 112.) Three of these transactions were made by Petitioner himself. Petitioner's expert witness based his entire valuation on these five transactions. However, under cross-examination, when asked if he received the 1985 financial statement for Computerland from Petitioner's attorneys, he stated, "I asked for them and did not receive them." (Transcript, p. 120.)

When asked if he understood that Computerland's 1985 after-tax earnings had dropped to $2,000,000, the witness responded that he "understood that the after-tax

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[1] This paid testimony comes despite the fact that under the terms of the note itself, that the Petitioner himself drafted, the Petitioner was given ninety (90) days to find a buyer for the collateral. No buyer was ever found by the Petitioner. As has been the story for eight (8) years now, nobody is "willing to pay" for this security despite what their expert testified to. In fact at the District Court appeal hearing the Respondent again offered the security back to the Petitioner for the principal and interest owed. As should come as no surprise the Petitioner rejected the offer.

had declined significantly" but stood by his paid evaluation. (Transcript, p. 121.)

It was clear that the Micro/Vest points had no market, representing nothing more than a claimed interest in a lawsuit that had yet to be won, a result that has not yet ever yielded any cash some eight (8) years after the loan had been made.

The only peculiar area of the Bankruptcy Court's findings was its dictum that supported this evaluation, which, of course, would ignore any standard valuation approaches, whether they be net worth analysis, book value analysis, market value analysis, price earnings analysis, cash flow analysis or comparative market analysis. It is inconceivable how this *infinitesimal fractional* interest (4/10ths of 1%) in a company with after-tax earnings of only $2,000,000 could possibly be worth $1,400,000 as the Bankruptcy Court noted in dictum. Petitioner "tags" his entire brief with result-oriented arguments, but should look at the Bankruptcy Court's dictum as pure result-oriented arguments, but should look at the Bankruptcy Court's dictum as pure result-oriented from the classic "give and take" now settled conclusion, something Petitioner has ignored.

Nonetheless, as the Bankruptcy Court found, Respondent was in possession of the security and had given proper notice under Section 9505(2) of retention of the security as satisfaction of the debt and such that any argument by Petitioner that he felt it was "too late" to object was "not credible." (Findings, p. 8.).

ARGUMENT

1. An Unpublished Opinion is Not the Type of Action by the Appellate Court that is "So Far Departed From the Accepted and Usual Course of Judicial Proceedings as to Call for an Exercise of this Court's Power of Supervision".

Petitioner's entire argument for this court to grant its Writ of Certiorari is based on Supreme Court Rule 10, which grants the court jurisdiction to hear matters where the United States Court of Appeals has rendered a decision that has "So far departed from the accepted and usual course of judicial proceedings . . . as to call for an exercise of this court's power of supervision." Rule 10(1)(a):

An unpublished decision that is well reasoned, as the case at hand, is not the type of departure that Rule 10 contemplates.

Ninth Circuit Rule 36-2 in pertinent part states:

> "A written, reasoned disposition shall be designated as an opinion *only* if it: (g) is accompanied by a separate concurring or dissenting expression, and the author of such separate expression requests publication of the disposition of the court and the separate expression. *FRAP* 36-2. (Emphasis Added.)

Although Judge Noonan of the Ninth Circuit dissented to the majority's opinion, he did so in only one sentence and did not request publication of the disposition of the court. If Judge Noonan really felt that this was a decision that was "So far departed from the accepted and usual course of judicial proceedings . . . as to call for

the exercise of this court's power of supervision, he certainly would have implemented Rule 36-2(g) and sought publication. However, Judge Noonan intentionally did not seek such a request as he knew this was a well settled area of law which does not have the judicial and social importance that Petitioner cries.

2. The Ninth Circuit's Opinion Does Not Establish, Alter, Modify, Criticize or Clarify Existing Law.

Although there were many issues that the lower court cited in favor of Respondent, the issue that Petitioner seeks is that of "possession" under California *Commercial Code* Section 9505(2). Petitioner suggests the Ninth Circuit somehow modified existing law to allow a general intangible to be possessed under California *Commercial Code* Section 9505(2), something Petitioner suggests *cannot* be possessed under California *Commercial Code* Section 9505(2).

However, the lower courts in this action and other legal authorities, have already ruled that such an intangible may be possessed for purposes of Section 9505(2).

In the law of secured transactions under the *Uniform Commercial Code*, 2d Ed, Section 4.10(3), pages 159-160, Clark states:

> "For another case that implies that retention and satisfaction of the debt is permissible even when the collateral is intangible, such as accounts receivable, see *In Re Emergency Beacon Corp.*, The clear implication from the case is that strict foreclosure would be available as an option for the accounts assignee." *Id.*, at 160 (*In Re Emergency*

Beacon Corp., 441 U.C.C. Rep. 1544 (jdn.y.1985) 481 BR 341. See *Grossman v. Lippson*, 81 Cal.App. 544, 146, Cal.Rptr. 741 (1978), where the court made it clear that a general intangible is capable of being possessed under the California *Commercial Code* wherein Grossman was allowed to repossess and take possession of all "intangible assets of the business", including the "good will." *Id.* at 744-45.

3. An Unpublished Decision is not Grounds for Writ of Certiorari.

In *Taylor v. McKeithen*, 407 U.S. 191, 92 S.Ct. 1980, 32 L.Ed.2d 648 (1972), a case cited by Petitioner, then Justice Renquist stated:

> "I think decisions as to whether opinions should accompany judgments of the court of appeals, and the desirable length and content of those opinions are matters best left to the Judges of the Courts of Appeals." *Id.* at 196. (Renquist dissenting). Justice Renquist went on to state:
>
> "No existing statute or rule of procedure prohibits the Fifth Circuit from issuing a short opinion and order, as it has done here, or from deciding cases without any opinion at all. *Cf. Rule 21, Court of Appeals for the Fifth Circuit.* The Courts of Appeal and particularly the Fifth Circuit, which has experienced the heaviest caseload of all the circuits, need the maximum possible latitude to deal with the 'flood tide' of appeals that the 'ever growing explosive increase' of federal judicial business has produced." *Id.* at 195-96, (See also *Isbell Enterprises, Inc. v. Citizens Casualty Co.*, 431 F.2d 409: *NLRB v. Amalgamated Clothing Workers*, 430 F.2d 966.)

4. A General Intangible is Clearly Capable of Being Possessed Under the California Commercial Code.

There is no question that a security interest can be created in a general intangible. Section 9102 defining the policy and scope of Division 9 states:

"This division applies (a) to any transaction (regardless of its form) which is intended to create a security interest in . . . general intangibles . . . " Section 9102.

The only formal requirement is the consensual intent by the parties to create a security interest. Once this intent is manifested, the next step in the blueprint is for the secured party to attach and then perfect his security interest so others cannot lay claim to the same interest or, in essence, to give the secured party priority.

Section 9203 entitled "Attachment and enforceability of security interest;" lays out three elements or prerequisites for attachment,

"(a) The collateral is in the possession of the secured party pursuant to agreement, or the debtor has signed a security agreement which contains a description of the collateral;

(b) Value has been given,

(c) The debtor has rights in the collateral . . .

Attachment occurs as soon as all of the events specified . . . have taken place." Section 9203.

It's important to note that the Code recognizes that possession does not have to be actual or literal, but rather can be pursuant to an agreement as illustrated in subdivision (1)(a).

However, once the security interest has been attached, the next step for the secured party is to perfect his interest in the security for two reasons. One, to give notice to third parties of his interest in the security, and two, to gain priority over any claims, by alleged bona fide purchasers as is illustrated by Section 9301 identifying persons who take priority over unperfected security interests.

When this is taken in context with the purpose of Division 9, which "is to cover (1) the creation of a security interest with priorities and (2) the giving of notice of a security interest to third parties," it is easy to see why the word "possession" was used by the drafters. *Article 9, Introductory Comment, West Annot., p. 282.* The rationale of the section is to protect third parties, not, as here, the Petitioner/Debtor who already has notice and by virtue of having drafted the document would be estopped to assert a defect in notice in any event.

Possession conveyed actual or constructive notice to *third* parties that someone besides the Debtor had a claim or possible claim to that interest. This puts the third party on notice that if he was thinking about taking a security interest in the property, he may be doing so with the risk that the Debtor has already pledged the property. With this notice, the third party could not become a bona fide purchaser or take priority over the original creditor.

However, the code also recognized that certain interests, general intangibles, could not ordinarily actually physically be touched, or were not ordinarily represented by a written notice (i.e., different from possession) and place a third party on effective notice that someone else

laid claim to that interest. Therefore, to remedy this situation the code required the secured party to file a financing statement with the Secretary of State, thereby placing all third parties on notice of the secured parties' interest in the collateral and establishing and/or guaranteeing his priority.

This is illustrated under the purposes of Section 9203 which states:

> "Perfection of a security interest (see Section 9303) will in many cases depend on the additional step of filing a financing statement (See Section 9302) or possession of the collateral (Section 9304(1) and 9304)." It only depends on the type of collateral held.

The Petitioner's argument misinterprets the purposes of Section 9305 by suggesting that a general intangible cannot be possessed. Nowhere in the purposes of Section 9305 do they indicate a general intangible cannot be possessed.

The purposes of Section 9305 only reiterate what certain types of collateral Section 9305 allow possession to perfect a security interest. It does not say a general intangible cannot be possessed. The purposes of Section 9305 state:

> "A security interest in accounts and general intangibles property not ordinarily represented by any writing whose delivery operates to transfer the claim may under this Article be perfected only by filing . . . " *Section 9305, Purposes.*

Section 9305 addresses the issue of "when possession by [a] secured party perfects [a] security interest without

filing". It does not indicate or suggest a general intangible cannot be possessed.

On the contrary, the Code expressly recognizes that a general intangible can be possessed, but because it is not "ordinarily represented by any writing whose delivery operates to transfer the claim," it may only be *perfected* by filing.

This is supported by *In Re S.O.A.W. Enterprises, Inc.*, 32 Banks 278, 37 U.C.C. Rep. Serv. (1983), which clearly found a general intangible possessable, but only capable of being perfected through filing.

The *Uniform Commercial Code Law Journal*, Vol. 23, No. 2, Page 189, citing the opinion of *S.O.A.W. supra*, stated:

> "Castle Rock had *possession* of the participation agreements in dispute. When the court concluded that Castle Rock's interest was a *general intangible*, its fate was sealed since perfection of a general intangible can only be accomplished through the filing of a financing statement. See *U.C.C.* Section 9305, Comment 1, showing how this conclusion is reached. Had the collateral been found to be other than a general intangible, or account, Castle Rock might still have prevailed if it could have established its possession as perfection." (*Id.* at 189, Footnote 18.) (Emphasis added.)

In addition, the purposes of Section 9305 refer the reader back to Section 9302(1) which addresses the issue of when filing is required to perfect a security interest.

Section 9302 specifically excludes an assignment of a beneficial interest in a trust from the filing requirements, clearly indicating that at least this type of intangible

collateral is capable of being possessed or its functional equivalent for the purposes of perfecting a security interest.

Section 9302(1)(c) specifically states:

> "(1) A financing statement must be filed to perfect all security interests *except* the following:
>
> (c) A security interest created by an assignment of a beneficial interest in a trust . . . " Section 9302(1)(c).

This section clearly indicates that a security interest in an assignment of a beneficial interest in a trust, a general intangible, is capable of being perfected without filing. In essence, indicating a general intangible is capable of being possessed.

The irony is this is the exact type of collateral, a beneficial interest in a trust, that Respondent foreclosed on under Section 9505(2).

Section 9505(2) deals with the "compulsory disposition" and "acceptance of the collateral as discharge of the obligation." In essence, it speaks to an interest that has already been attached and perfected and has now entered into default.

In dealing with these very issues in *Grossman v. Lippson*, 81 Cal.App. 554, 146 Cal.Rptr. 741 (1978), the court made it clear that a general intangible is capable of being possessed under the California *Commercial Code*.

Grossman owned and operated the Mediterranean carwash which was subsequently subleased to the defendant and debtor Lippson. After Lippson's default on the equipment lease and promissory note, Grossman "took

possession of the carwash business, equipment and premises" and subsequently filed suit against Lippson for the unpaid balance of the note. The court specifically stated:

> "The transfer took the form of a sublease of the underlying real property: the lease purchase of carwash equipment, and a sale of the goodwill, tradename and other *intangible* assets of the business." *Id.* at 744. (Emphasis added.)

The court continued to state:

> "Yet what was sold was a package – one that included goodwill, tradename, *intangibles*, improvements, fixtures, premises, and carwash equipment, all the elements needed to conduct the business. On default, the seller *repossessed* the entire package – premises, equipment, and business . . . " *Id.* at 745. (Emphasis added.)

The court continues to make the issue of possession of a general intangible expressly clear by stating:

> "When the business fell on hard times, land, equipment, and the on-going business were all simultaneously repossessed by the seller-creditor." *Id.* at 745

Here, the general intangibles are the components of the "on-going business," in essence the goodwill, tradename and other intangibles of the business. In interpreting the California *Commercial Code*, the court stated:

> "Accordingly, when the creditor *repossessed* all three components of the enterprise's (premises, equipment and on-going business) the debtor became entitled to receive credit against the unpaid balance of the promissory note for the value of each of the three components

> *repossessed*, which together constituted the security for the debt." *Id.* at 747.

Here the court is making it abundantly clear that a general intangible under the California *Commercial Code* can be possessed as was illustrated by *Grossman* repossessing the general intangibles of the on-going business of the Mediterranean carwash. In *The Law of Secured Transactions Under the Uniform Commercial Code*, 2nd Ed., Section 4.10[3], pp. 159-160, *Clark* states:

> "For another case that implies that retention and satisfaction of the debt is permissible even when the collateral is intangible, such as accounts receivable, see *In Re Emergency Beacon Corp.* The clear implication from the case is that strict foreclosure would be available as an option for the accounts assignee." *Id.* at 160.

In Re Emergency Beacon Corp., 441 U.C.C. Rep. 1544 (JD N.Y. 1985), 48 BR 341, the debtor, Emergency Beacon, received a loan from Montco that was secured in part by Beacon's accounts receivable, a general intangible.

To satisfy the debt, *Beacon* turned over to Montco the accounts receivable.[2] The court then specifically states that *"Montco acquired possession"* of the accounts receivable. *Id.* at 346. A general intangible.

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[2] Here, *Beacon* gave possession of the accounts receivable to Montco without a 9505(2) notice of retention. The court held that a turnover of accounts receivable to the secured creditor did not constitute an implied satisfaction of the entire debt owed to Montco because no notice was given as required under 9505(2).

In Re Emergency Beacon Corp. makes it clear by its express language that a general intangible can be "acquired" and therefore, "taken possession" of under Section 9505(2).

This is further supported by the express purpose of Section 9505(2) as stated in the *Code Comment*.

> "Purposes: (1) Experience has shown that the parties are frequently better off without a resale of the collateral: hence this section sanctions an alternative arrangement. In lieu of resale or other disposition, the secured party may propose under subsection 2 that he keep the collateral as his own, thus discharging the obligation and abandoning any claim for a deficiency." *Code Comment* Section 9505(2).

The code recognizes that some types of collateral are unique in nature and not the type frequently sold on a common market. Therefore, to avoid the uncertainties and hassles of fulfilling the obligations of what is and is not a commercially reasonable manner in a collateral that is unique and does not have a ready and common market, the code sanctions an alternative arrangement; in essence, proposing to retain the collateral as satisfaction of the debt.

The code purpose gives no hint or suggestion that a general intangible cannot be possessed. To somehow suggest that a general intangible should be excluded from Section 9505(2) would be contrary to the code purpose, in essence, allowing an alternative arrangement to Section 9504.

As the trial court so eloquently stated:

> "Section 9505(2) does not limit its applicability to certain types of collateral. Indeed, the reach of the Commercial Code otherwise extends to both the creation and enforcement of a security interest in general intangibles. It would violate basic principles of statutory construction to read this form of collateral out of Section 9505(2)." (Findings, pp. 6-7.)

Even the District Court has stated that Petitioner's argument must fail because:

> "Section 9505(2) does not limit its application to certain kinds of collateral. There is nothing in either Sections 9505(2) or 9504, or the comments to those sections, which specifically limits the application of Section 9505(2) as debtor suggests." (Opinion, P.5)[3]

The Ninth Circuit agreed citing *Kruse, Kruse & Mikolsko v. Beedy*, 353 N.E. 2nd 514, 539 (Ind.App. 1976) as applicable when *Kruse* found that:

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[3] The District Court further held that the debtor's argument must fail because the "bankruptcy judge found that while Appellee may not have been in actual possession of the collateral, it had sufficient dominion and control over it to constitute 'possession' for purposes of § 9505(2)." This holding was based on a finding that the trustee to the trust acknowledge Appellee's control over the two percent (2%) interest in a letter to Appellee dated July 16, 1984, in which the trustee recognized that Debtor had "transferred an interest" in the trust and agreed to "act in accordance with writings from your office regarding disposition of said two percent undivided beneficial interest." (Opinion, pp. 5-6)

> "Possession of collateral by a bailee who has received notification of the interest of a secured party is considered to be possession by the secured party." *Id.* at 539.

The Ninth Circuit found this case analogous because the Trustee of Micro/Vest, acting as bailee for Respondent, had acknowledge possession by a letter to all interested parties. (Pet. Brief 26a)

Therefore, all three lower courts have sided with Respondent and the applicable case law and have found that a general intangible is capable of being possessed for purposes of Section 9505(2).

5. The Respondent Has Properly Foreclosed Under Section 9505(2) Because the Petitioner Has Failed to Object in Writing within 21 Days of Notice.

Section 9505(2) follows the agreement's terms and allows the secured party after default to *propose* to retain the collateral in satisfaction of the debt. If the debtor disagrees with this proposal and wants the collateral disposed of under Section 9504, then he must state his objections *in writing* within 21 days of the notice of proposal sent by the secured party. Section 9505(2).

"When an objection is received by the secured party he must then proceed to dispose of the collateral in accordance with Section 9504 . . . " otherwise he may retain the collateral in satisfaction of the debt. *Code Comment, Purposes 9505(2).*

The *code* specifically states that, "In the absence of such written objection the secured party may retain the

collateral in satisfaction of the debtor's obligation." Section 9505(2).

The record is clear. There was never a written objection sent by Petitioner, let alone within the 21 days required by the code. In fact, not even a hint of objection to the retention was even received by Respondent until approximately five years later when Petitioner filed suit. (Transcript and Findings, p. 8).

As rightfully stated by the trial court:

> "Had he [Petitioner] sent a written objection within the 21 day period prescribed by the statute, he might now be in a position to assert his rights under Section 9504. Having failed to object, he lost that right, and the foreclosure became valid." (Findings, p. 8). Both the District Court and Ninth Circuit joined in this reasoning.

The code makes it clear that if the debtor does not object in writing within the 21 days, he has waived any right that would require the secured party to proceed under Section 9504. The same is necessarily true that the debtor has waived his right to object that the secured party was not in possession of the collateral. As indicated in *8 U.C.L.A. Law R. 953*, "By not objecting to the secured party's proposal to retain the collateral, the debtor relinquishes any claim to the surplus proceeds." *Id.* at 953.

It is obvious the 21 day period was established to allow the secured party to rely on the Debtor's lack of objection, so the secured party could then proceed with the collateral as he sees fit. To allow the Debtor to object after the 21 day period would have a secured party in a

state of flux and uncertainty as to the collateral and at the mercy of the Debtor. This is supported by *8 U.C.L.A. Law R.* (*supra*), which states, "If the proposal is accepted by the debtor and others with an interest, the secured party is free to deal with the security as he wishes. . . . " *Id.* at 953.

By the Debtor's (Petitioner's) lack of written objection within the 21 days prescribed by Section 9505(2), Respondent has properly foreclosed. Debtor cannot sit back, wait to see what happens to the property, and then make an objection five years later, claiming a ridiculous value that *never* existed. Especially when Debtor was offered and re-offered the stock for simply what was owed. No answer for years! Now he has an objection.

6. The Respondent Gave Proper Notice of a Proposal to Retain the Collateral in Satisfaction of the Debt.

On March 13, 1985, Respondent sent notice to Petitioner that he was delinquent on payment per the terms of the note.

The note, *drafted by the Petitioner himself, specifically allowed* Respondent to retain the collateral in satisfaction of the debt if a buyer for the security could not be located by either Respondent or Petitioner within 90 days of the March 3, 1985 notice.

The note specifically states that after notice of delinquency is sent:

> "The holder shall have 90 days from the date of such demand within which to locate a buyer or

> buyers and complete said sale. I (Petitioner) agree to assist the holder in locating a buyer and in closing such transaction . . . In the event the holder is unable to arrange one or more transactions yielding enough to cover such claim, I shall have the right, during 90 days from the date of the notice of delinquency, to arrange for such transaction myself. *In the event transactions of sufficient size are not arranged by the holder or by me, then on the 91st day after the date of the notice, full title to said security shall transfer to the holder and shall be deemed full satisfaction of the entire obligation: I shall not be liable for any real or alleged deficiency."*

Therefore, by the specific terms of the note which the Petitioner himself drafted, he eliminated the danger of a deficiency and agreed that he was placed on notice that if a sale could not be arranged, either by Respondent or Petitioner, that Petitioner would then strictly foreclose under Section 9505(2).

In addition, it was made perfectly clear to Petitioner that Respondent would not sell the collateral but rather, elect to retain the collateral in satisfaction of the debt when it stated in its March 13, 1985 letter that, *"We certainly do not wish to exercise our right of conversion. We just want to get paid back and alleviate the bank's fiduciary concerns."*

Furthermore, the same proposal was sent to Petitioner, *five months later,* on August 13, 1985, when Respondent stated:

> "As has been communicated to you several times, this is not a security we can sell. This is especially true in light of the lawsuits against

> Micro/Vest. We cannot subject the pension plan participants to exposure to multi-million dollar lawsuits over the sale of the security.
>
> Furthermore, since your efforts to sell the security have been unavailing, efforts which we appreciate have been made more difficult by the lawsuits, and since we owe the utmost fiduciary duty to our plan participants, the plan has foreclosed on the security."

By the express language of the August 13, 1985 letter, the Petitioner was clearly on notice that the Plan would not and could not sell the security.

The same concern Respondent had been communicating to Petitioner about the difficulties of selling such a security including the potential liabilities that existed were conveyed in the *Uniform Commercial Code Law Journal*, Vol. 6, No. 1404, page 339, when it stated:

> "Section 9505(2) is often employed, for example, in cases of disposition of unregistered securities whose public sale under Section 9504(3) would be fraught with difficulty." *Id.* at 339.

Although Respondent believes this language is more than clear that Respondent would be retaining the collateral as satisfaction of the debt, it, at the very least, would put a reasonable person on notice that Respondent was proposing to retain the collateral in satisfaction of the debt.

The trial court agreed by stating:

> "Even if the August 13, 1985 letter was not in the nature of a proposal, I find that the March 13, 1985 letter can be fairly read as being one. Consistent with their agreement, Martin was

> given 90 days to find a buyer on the two points. During that time, he must surely have been aware of the fact that the plan was doing nothing to sell the note, and probably intended to keep it." (Findings, pp. 8-9.)

In fact, the trial court, after listening to the testimony of Petitioner, stated:

> "While the letter does state that the foreclosure is final 'with title vested in the pension plan,' the fact remains that, thereafter, Martin did nothing to protect the loss of the 2%. *His half-hearted assertion that he felt it was too late is not credible,* particularly in light of defendant's August 25th letter which left the door open for Martin to repurchase the 2% for the principal and interest owing." (Findings, p. 8.)

Petitioner's credibility as determined by the trial court is a question of fact that should be viewed under the clearly erroneous standard. *In the Matter of Pizza of Hawaii, Inc.*, 761 F.2d 1374, 1377 (9th Cir. 1985). Even the District Court stated:

> "The bankruptcy court's finding on the notice issue presents questions of fact which are reviewed under the clearly erroneous standard. Here, the March 13th letter clearly gave notice that Debtor was in default. Additionally, as the bankruptcy court found, the letter indicated that Respondent did not wish to exercise its right to conversion. The court found that this letter was sufficient notice. The fact that Debtor did nothing to address this issue, despite repeated requests, further supports the bankruptcy court's findings."

The Ninth Circuit agreed by pointing to the March 13, 1985 letter and stating:

> "This letter specifically indicates that the plan is giving 'notice pursuant to the terms and conditions of the note'. Pursuant to the agreement, debtor was given 90 days to find a buyer for the two percent. The Bankruptcy Court found that debtor 'neither found a buyer, nor paid off the note, nor protested the impending foreclosure called for in the agreement.' " (Pet. Brief 26a)

Respondent even gave Petitioner 60 more days to find a buyer or buy back the two points for just the principal and interest owed. The Ninth Circuit found that the:

> "Bankruptcy judge's determination that notice was given was not clearly erroneous."

In fact, the Ninth Circuit held that:

> "Even if we review de novo reasonableness of notice as a matter of law, as debtor urges, we find the three letters sent to debtor over a six month period constituted notice that the Plan was proposing strict foreclosure." (Pet. Brief 26a)

It is clear that the trial court, District Court and Ninth Circuit Court have determined that the March 13, 1985 letter did represent a proposal. The fact that Petitioner argues that the March 13, 1985 letter was not in the nature of a proposal, but rather a final statement:

> "Is not credible, particularly in light of defendant's August 25th letter which left the door open for Martin to repurchase the 2% for the

principal and interest owing." (Findings, pp. 8-9.)

Petitioner was given numerous opportunities to repurchase the collateral for the principal and interest owing, however, Petitioner never responded to such offers, let alone object that a foreclosure was improper.

Therefore, it is clear that under the terms of the note which Petitioner himself drafted, the March 13, 1985, August 13, 1985, and the August 25, 1985 letter, that Petitioner was well aware that the Plan intended on retaining the collateral in complete satisfaction of the debt. Petitioner's argument that he felt it was too late to object to Respondent's retention is simply "not credible."

CONCLUSION

For the reasons set forth above, the Respondent herein submits that a Writ of Certiorari should not be granted in this case.

DATED: July 8, 1994

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